

EXHIBIT H

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**Republic of Congo: 2004 Article IV Consultation and New Staff-Monitored Program—
Staff Report; Staff Statement; Public Information Notice on the Executive Board
Discussion; and Statement by the Executive Director for the Republic of Congo**

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2004 Article IV consultation with the Republic of Congo and a new staff-monitored program, the following documents have been released and are included in this package:

- the staff report for the 2004 Article IV consultation and a new staff-monitored program, prepared by a staff team of the IMF, following discussions that ended on March 5, 2004, with the officials of the Republic of Congo on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on May 12, 2004. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.
- a staff statement of June 10, 2004 updating information on recent developments.
- a Public Information Notice (PIN) summarizing the views of the Executive Board as expressed during its June 10, 2004 discussion of the staff report that concluded the Article IV consultation.
- a statement by the Executive Director for the Republic of Congo.

The documents listed below have been or will be separately released.

Letter of Intent sent to the IMF by the authorities of the Republic of Congo*
Memorandum of Economic and Financial Policies by the authorities of the
Republic of Congo*

Selected Issues Paper and Statistical Appendix
Technical Memorandum of Understanding*

*May also be included in Staff Report

The policy of publication of staff reports and other documents allows for the deletion of market-sensitive information.

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INTERNATIONAL MONETARY FUND

REPUBLIC OF CONGO

**Staff Report for the 2004 Article IV Consultation and
a New Staff-Monitored Program**

Prepared by the African Department and Policy Development and Review Departments

(In consultation with the External Relations, Finance, Fiscal Affairs, Legal, Monetary and Financial Systems, and Statistics Departments)

Approved by Menachem Katz and Anthony Boote

May 12, 2004

- The discussions for the 2004 Article IV consultation with the Republic of Congo (hereafter “the Congo”) were initiated in Brazzaville during February 5-20, 2004 and completed at headquarters during March 1–5, 2004. The letter of intent (LOI) dated March 31, 2004 outlines the government’s policies during January–June 2004 under the 2004 staff-monitored program (SMP).
- The staff team consisted of Messrs. Ghura (Head), Karangwa, Leite, Ms. Linares (Administrative Assistant) (all AFR), Mr. Op de Beke (PDR), and Mr. Moussa (FAD). Staff members from the African Development Bank (AfDB) and the World Bank participated in the discussions.
- The mission met with President Sassou-Nguesso; the presidents of the national assembly and the senate; Mr. Andély, Minister of Economy, Finance, and Budget; Mr. Moussa, Minister of Planning; Mr. Dzon, National Director of the Bank of Central African States (BEAC); other senior officials; and representatives of civil society and the donor community.
- At the conclusion of the 2003 Article IV consultation on June 13, 2003 (Country report No. 03/193), Directors noted that performance in 2002 was disappointing, despite favorable oil prices, and expressed concern about the deterioration of the fiscal position. However, they welcomed the new government’s focus on reestablishing fiscal discipline and were encouraged by the improved performance during October 2002–March 2003. As for the length of the performance track record needed for consideration of an arrangement supported by the Poverty Reduction and Growth Facility (PRGF), Directors favored a 12-month period under an SMP ending in September 2003.
- The Congo is on the standard 12-month consultation cycle, and together with other members of the Central African Economic and Monetary Community (CEMAC), has accepted the obligations of Article VIII, Sections 2, 3, and 4 of the Fund’s Articles of Agreement. Congo’s relations with the Fund are summarized in Appendix I.

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EXECUTIVE SUMMARY

Background

- **The gradual reestablishment of political stability and democratic institutions over the past four years has generated a sense of guarded optimism** that the Congo is on the cusp of a structural break from the previous pattern of intermittent outbreaks of civil conflict. Over the past year, security improvements have been consolidated by the launch of the demobilization program for former combatants, and further progress has been registered with respect to the reestablishment of democratic institutions.
- **The onset of peace in 1999–2000 has boosted the pace of economic activity in the non-oil sector.** Consumer price inflation has abated in the post-conflict period, partly due to a more reliable supply from Pointe-Noire to Brazzaville. In an encouraging sign of a pickup in non-oil sector activity, credit to the economy grew in 2003 at a faster rate than non-oil GDP for the first time in three years. Nonetheless, key social indicators have continued to deteriorate, and the external debt burden is heavy.
- **The completion of the transition period to a democratic state and the gradual return to peace, thus far, has not been accompanied by the strict implementation of economic programs.** Since 2000, one post-conflict emergency assistance and three subsequent staff-monitored programs(SMP) have not led to a medium-term program supported by the Poverty Reduction and Growth Facility (PRGF).
- **Performance under the 2003 SMP, covering the period January–September, was weak.** While overall fiscal performance improved in 2003, key budget targets, including on non-oil revenue and expenditures, were missed. Continued weaknesses in treasury management necessitated the deferment of oil-collateralized debt to 2004. Although some key structural measures were not implemented, an effort to improve transparency in the oil sector was launched under the SMP and reinforced in the fourth quarter.

Article IV consultation issues

- **The discussions focused on the following key medium-term issues:** (i) improving governance and transparency, starting with the oil sector; (ii) ensuring long-term fiscal sustainability; (iii) strengthening public expenditure management and institutional capacity; and (iv) creating favorable conditions for private sector expansion and poverty reduction.
- **The key policy challenges** will be to enhance fiscal discipline while facing pressures for “peace dividends,” implement oil sector reform measures that may run counter to vested interests, and improve the statistical infrastructure in the face of significant institutional capacity constraints.
- **The authorities intend to establish the necessary track record to move to a possible PRGF-supported program** by satisfactory implementation of an SMP during

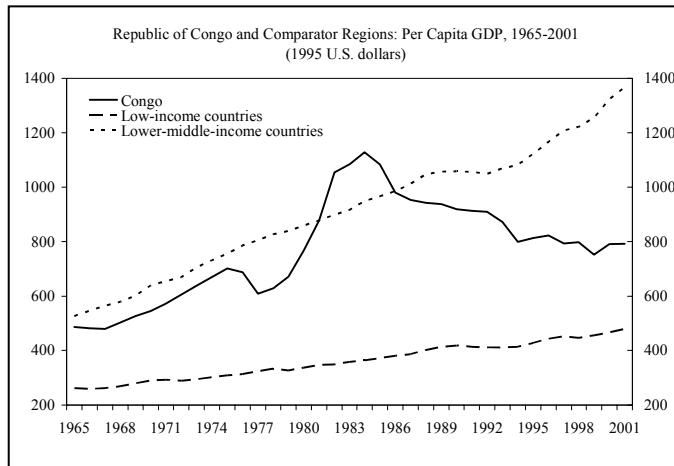
January–June 2004. The key objectives are to strengthen the framework for fiscal discipline and enhance oil sector transparency.

Issues stressed in the staff appraisal

- **The staff is encouraged by the recent progress on the security and political fronts.** Accompanying this positive momentum, the staff welcomes the pickup in economic activity in the non-oil sector and deceleration of inflation. Nonetheless, the implementation of the 2003 SMP was weak and did not allow the Congo to move to a medium-term program supported by the international community.
- **The staff regrets the opportunity missed in 2003 by not using additional oil revenues to clear a significant amount of external arrears.** The staff urges the authorities to use future additional oil revenues in accordance with stated program objectives and priorities.
- **The staff is encouraged by the authorities' renewed determination to strengthen the framework for moving to a medium-term program** for growth and poverty reduction that can be supported by the international community. The program for 2004 appropriately addresses the most pressing issues facing the Congo, and the authorities are encouraged to diligently implement the proposed measures.
- **The implementation of the SMP would be a necessary, but not sufficient, condition for moving to a PRGF-supported program.** The Congo would also need exceptionally favorable treatment on arrears to official bilateral and commercial creditors on post-cutoff-date debt and to multilateral creditors. To improve the credibility of the government's strategy, the staff urges the authorities to take decisive steps in improving transparency and accountability in the oil sector, and in mobilizing maximum domestic resources and utilizing them judiciously.
- **The Congo is faced with daunting challenges in moving onto a sustainable path of economic development.** Increased focus on oil sector transparency and governance should be a key aspect of a strategy to lower the probability of future conflicts and to strengthen the decision-making process. Another key challenge is to improve the business climate by, *inter alia*, enhancing the overall governance framework and effectively combating corruption, and improving the efficiency in the delivery of public utility services.
- **Timely provision of reliable economic and financial data is essential for effective macroeconomic management and Fund surveillance.** The provision of comprehensive information, including on oil-related activities, will help to convince development partners that domestic resources are being fully mobilized and will lend credibility to the ongoing reform efforts.

I. INTRODUCTION

1. The Congo is emerging from three intense civil conflicts in the 1990s. Once classified as a lower-middle-income economy, the Congo has experienced a continuous decline in per capita income over the past 15 years or so (see accompanying figure). This negative trend coincided with the overvaluation of the CFA franc in the second half of the 1980s, three conflicts in the 1990s, an acceleration of rural to urban migration in the 1980s, and continuing institutional weaknesses.



2. The post-conflict period ushered in by the 1999 cease-fire agreement has been conducive to the installation of democratic institutions but, thus far, has not been accompanied by the strict implementation of economic programs. Over this period, the program launched in November 2000 under the post-conflict emergency assistance and three subsequent staff-monitored programs (SMPs) have not been successful in laying the foundations for moving to possible support under the Poverty Reduction and Growth Facility (PRGF). Nevertheless, the combination of a steadily improving security situation and some encouraging results under the 2003 SMP have generated cautious optimism that a virtuous circle of political stability and economic reform has been set in motion.

3. The World Bank has also been involved in Congo's postwar economic recovery efforts. Currently, an Economic Recovery Credit amounting to US\$30 million is under preparation. Appendix II summarizes Congo's relations with the World Bank Group.

II. POLITICAL, SOCIAL, AND ECONOMIC BACKGROUND

4. The enormity of the destruction left by the successive and intense rounds of civil wars (1993, 1997, and 1998–99) has been revealed as the security situation improved. Key social and economic indicators have deteriorated or stagnated in the 1990s, and the external debt burden is heavy (see Table 1 below). Over 70 percent of the population lives below the poverty line, according to World Bank estimates.

Table 1. Republic of Congo: Selected Economic and Social Performance Indicators, 1980-2003					
	1980-84	1985-89	1990-94	1995-99	2000-03
National accounts	(In percent, unless otherwise indicated)				
Per capita GDP (in 1995 U.S. dollars)	982	979	883	796	791
Real GDP growth	14.3	-0.7	-0.1	1.7	4.1
Oil	12.5	9.3	3.8	9.1	-4.3
Non-oil	14.9	-3.3	-1.7	-2.8	10.3
Consumer price inflation	3.7	-2.8	9.0	7.4	1.6
Fiscal accounts	(In percent of GDP, unless otherwise indicated)				
Total domestic revenue (excluding grants)	34.1	25.8	24.3	25.7	28.4
Primary expenditure and net lending 1/	24.3	22.9	26.4	21.6	22.6
Basic primary budget balance	9.8	2.9	-2.2	4.2	5.8
External sector					
Trade balance	23.3	25.6	24.3	40.1	51.6
External debt	89.6	176.6	217.5	236.9	180.8
Real effective exchange rate (index, 1990=100)	96.7	98.8	92.7	79.3	80.2
Terms of trade (index, 1990=100)	179.6	125.8	84.1	78.0	124.2
Social indicators	(In units indicated)				
Adult illiteracy ratio (in percent of people age 15 and above)	46	38	30	23	19
Secondary school enrollment ratio 2/	74	75	54	53	42
Immunization ratio 3/	50	70	67	33	31
Life expectancy at birth (in years)	50	51	51	51	51
Sources: Congolese authorities; and staff estimates and calculations.					
1/ Noninterest current expenditure plus domestically financed investment.					
2/ In percent of the number of children of secondary school age.					
3/ In percent of the number of children under 12 months for immunization against diphtheria, tetanus, and polio.					

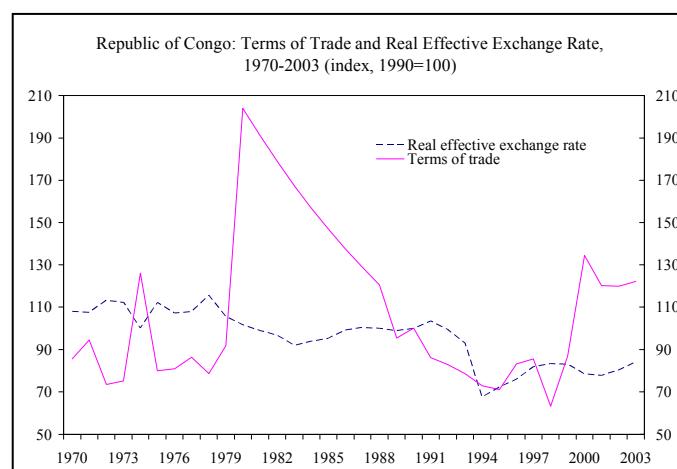
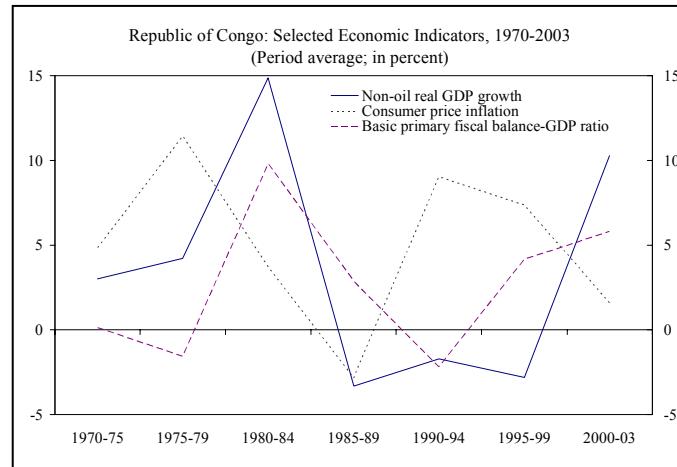
5. Recent developments on the security front are helping to consolidate the stability and peace achieved by the 1999 ceasefire and the 2002 elections:

- A March-2003 peace accord with the remaining rebel group, recommitting both sides to the terms of the 1999 cease-fire, was followed by the approval in August of amnesty provisions for both rebel and government combatants.
- With security restored in the area surrounding Brazzaville—the Pool region—the reliability of the vital rail link between Pointe-Noire (port city) and Brazzaville (administrative capital) has improved.
- In November 2003, President Sassou-Nguesso signed into law the program for demobilization, disarmament, and reinsertion of former combatants.

6. To help convert these gains into lasting political stability, efforts are under way to strengthen the institutional framework by nominating officials and allocating budgetary resources for the Court of Accounts, the Economic and Social Council, and the

Constitutional Court. The authorities stated that the bulk of the spending on post-conflict reconstruction, security, and elections was being financed from their own resources and oil-backed borrowing. They explained that a large part of the discrepancy in oil revenues recorded during 1999–2001 (about CFAF 174 billion) was used outside the usual budgetary process, principally to finance reconstruction and humanitarian projects, as well as sovereignty-related outlays, such as elections, security, and national reconciliation (Box 1).

7. The onset of peace in 1999–2000 boosted economic activity and contributed to macroeconomic stability during 2000–03 (Table 1 above; and Table 7). Non-oil real GDP increased by about 10 percent per annum on average during 2000–03. Consumer price inflation decelerated significantly, helped by a more reliable supply from Pointe-Noire to Brazzaville and a strengthening of the euro. The real effective exchange rate in the post-conflict period remains about 10–15 percent below its pre-1994 devaluation level, despite the recent rise in the terms of trade and the strengthening of the euro (see accompanying figure).



III. PROGRAM IMPLEMENTATION AND ECONOMIC DEVELOPMENTS IN 2003

8. Building on the momentum generated by the improvements on the political and economic fronts, the government began focusing on economic management in late 2002. To pave the way for a move to a PRGF-supported program, the authorities implemented an SMP in 2003, initially covering the period January–June and then extended to September 2003. Overall performance under the SMP was weak, but the authorities took steps, especially later in 2003, to enhance transparency and governance in the oil sector and to strengthen public finance management (Box 2).

9. The Congo benefited in 2003 from a favorable international oil market but a somewhat slower-than-projected pace of domestic economic activity. The world oil price averaged US\$29 per barrel (compared with US\$22 per barrel in the budget), but this was

partially offset by the weakening dollar (with the CFA franc per U.S. dollar exchange rate about 15 percent lower than programmed). Real GDP grew by 1 percent (compared with 2 percent in the budget), owing principally to lower-than-projected oil production. Non-oil real GDP growth slowed to 5.8 percent (from 6.7 percent in 2002) as the “catch-up” factor to a more normal pace of economic activity in the post-conflict period began to taper off.

Box 1. Oil Revenue Discrepancy, 1999–2001

The 2003 Article IV consultation (Country report No. 03/193, para. 9) identified a shortfall of some CFAF 174 billion in oil revenues over the period 1999–2001. This gap related to a discrepancy between revenues recorded by treasury and tax liabilities of the oil companies as stipulated in the production-sharing contracts. Although the 1999–2001 external audit of the national oil company (SNPC) was expected to shed light on this issue, the auditors were not granted access to the underlying documentation and were thus unable to reach any conclusions.¹ The government committee charged with explaining the discrepancy was able to verify approximately half of the shortfall, as follows:

Explanation/Item	Percent of shortfall
Nonpayment by CORAF of crude oil deliveries	12
Losses on fixed-price three year forward sale	13
Losses due to sales by the SNPC below reference price	23

The remainder of the discrepancy could not be verified. Off-budget expenditures, carried out by the SNPC on behalf of the government, were estimated to total 30 percent, as follows:

Explanation/Item	Percent of shortfall
Construction projects	10
Security-related expenditures	7
Peace initiatives	6
Humanitarian aid	4
Financing charges	3

Budget expenditures, identified ex post, were estimated to total 8 percent. The residual, 15 percent of the discrepancy, could not be verified or explained.

¹ The terms of reference for the external audit included an examination of the fiscal agency role of the SNPC and an audit of expenditures carried out on behalf of the government. Because of concerns of national security, the auditors were not allowed access to the invoices and bank statements necessary for these evaluations.

Box 2. Program Implementation in 2003

Overall performance under the 2003 SMP (covering January-September 2003) was weak:

- **The primary fiscal surplus fell short of the program target** by some CFAF 57 billion (equivalent to 2.8 percent of annual GDP). The main reasons included (i) a significant shortfall in non-oil revenue, (ii) retention of tax obligations by the national oil company (SNPC), and (iii) unprogrammed expenditures. Additionally, exceptional oil receipts¹ and unprogrammed oil bonus and dividend receipts were effectively used to clear unprogrammed internal arrears.
- **On the structural front, performance was mixed.** The audit of the SNPC for 1999-2001 was completed, efforts were made to centralize government revenues, no new oil-collateralized debt was contracted, and initiatives were launched to publish oil sector data. Nonetheless, not all nonreschedulable debt service was paid, the privatization of the remaining publicly owned bank (CAIC) was not completed, and the end-September 2003 measures on oil sector transparency were not implemented.

The authorities had set quantitative and structural targets in the last quarter of 2003 with a view to stabilizing the fiscal slippages registered under the SMP and further enhancing transparency and governance in the oil sector:

- **On the fiscal front**, the basic primary budget balance objective (which had been revised downward) was met. Nonetheless, unprogrammed outlays were made on clearance of pension arrears and the financing of structural reform costs.
- **On the structural front**, a significant step was taken to enhance transparency in the oil sector with the completion of the certification, by an external auditor, of government oil revenue for the period January-September 2003. Measures in the fiscal area included (i) the appointment of new directors in the General Directorates of Budget, Customs, and Taxes, as well as at the General Inspectorate of Finance, in order to reinvigorate the revenue departments and strengthen control; (ii) the signing of an agreement among the government, SNPC, and CORAF, to have the latter pay for its purchase of government crude oil; and (iii) the production of the 2000 budget review law (*Loi de règlement*).

¹ Resulting from the settlement of a legal dispute with a private oil company (see para. 13) .

10. The fiscal position in 2003 improved from the exceptionally poor performance of 2002, but the underlying fiscal effort was weak relative to the 2003 budget (Table 2; and Table 8). Higher-than-budgeted oil revenue together with lower-than-budgeted investment and interest expenditures generated a significant improvement in the overall fiscal balance in 2003. However, effective budget execution was hampered by weaknesses in expenditure controls, ineffectual treasury management, and delays in the implementation of non-oil revenue measures. Nonetheless, measures were taken later in 2003 to start correcting these deficiencies (Box 2).

11. In an encouraging sign of a pickup in non-oil sector activity, credit to the economy grew in 2003 at a faster rate than non-oil GDP for the first time in three years (Table 9). Bank deposits decreased by 8 percent in 2003, partly in response to the difficulties in effecting current transfers (Box 3) and the diminished confidence in the remaining state-owned bank, Crédit pour l'Agriculture, l'Industrie et le Commerce (CAIC). Overall, the banking system remains fragile as, in addition to the CAIC, two out of the other three commercial banks have failed to meet some of the key prudential ratios.

Box 3. Control by the Regional Central Bank of External Transfers, 2003

Monetary developments in 2003 were marked by the regional central banks (BEAC)'s tightening of controls on external transfers, a response to low external reserve coverage in the Republic of Congo. Over the first half of 2003, the Congo suffered a sharp decline in reserves with the currency cover ratio¹ falling below the minimum threshold of 20 percent in April; the primary cause of the sudden drop was a large outflow, including to service external debt.

In tightening control, the BEAC set a ceiling above which transfers require the prior written consent of its headquarters. In the case of the Congo, the ceiling was progressively lowered until reaching zero in June 2003; public sector transfers were excluded from these controls. The local BEAC authorities assured the mission that this process did not cause undue delays in effecting current transfers.

¹ Calculated as the ratio of gross official assets to short-term liabilities of the central bank.

Table 2. Republic of Congo: Central Government Operations, 2000-03					
	2000	2001	2002	2003	
(In percent of GDP)					
Domestic revenue (excluding grants)	26.3	30.7	27.2	28.0	29.6
Oil	20.3	21.1	18.9	17.8	20.7
Non-oil	5.9	9.7	8.3	10.2	8.9
Total expenditure and net lending	25.5	31.6	35.4	26.9	29.7
Primary expenditure	17.9	23.9	26.0	19.0	22.8
Current (excluding interest due)	11.6	14.1	18.4	14.2	17.3
Domestically financed investment	6.3	9.8	7.6	4.8	5.5
Interest due	6.9	7.4	8.4	5.2	5.8
Foreign-financed investment	0.6	0.2	1.1	2.8	1.2
Overall fiscal balance	0.8	-0.9	-8.2	1.1	-0.1
Basic primary fiscal balance 1/	8.4	6.8	1.2	9.3	6.8
(In percent of non-oil GDP)					
Non-oil revenue	17.3	22.3	17.8	22.0	17.6

Sources: Congolese authorities; and Fund staff estimates.

1/ Domestic revenue (excl. grants) minus primary expenditures.

12. The external current account deficit remained relatively unchanged, at 0.3 percent of GDP, in 2003 (Table 10). The decline in oil export value¹ was offset by lower government imports and interest due on external debt. In the non-oil sector, exports of tropical wood increased significantly as new production capacity came on-line. Efforts were undertaken in 2003 to start normalizing relations with external creditors by (i) remaining current on debt-service payments to multilateral institutions and Paris Club creditors (with the exception of one bilateral creditor) on post-cutoff-date debt, and (ii) clearing arrears (of about US\$12 million) to a few multilateral creditors. The Congo remains a heavily indebted country, with an external debt stock equivalent to about 185 percent of GDP at end 2003, two-thirds of which represents arrears (Table 11).

13. The Congo missed an opportunity to normalize relations with external creditors by not using additional oil revenue received in 2003, equivalent to some 5 percent of GDP, for the clearance of a larger amount of arrears owed to them (Table 3).

Additional oil revenue stemmed from higher-than-budgeted world oil prices and a one-time bonus (about 2 percent of GDP), and the proceeds of the settlement of a legal dispute with an international oil company (about 3 percent of GDP)—see Box 4 on the nature of this settlement. A portion of these resources (1.7 percent of GDP) was automatically transferred to cover costs associated with the Nkossa field (in accordance with existing contracts). The bulk of the remaining resources was used primarily to finance an ex ante budgetary gap, clear domestic arrears on large commercial claims, and clear domestic priority arrears (related to salaries, pensions, and small- and medium-sized enterprises).

14. The record on the government's nonbank privatization program was mixed in 2003. A core component of the strategy was to place the distribution of water and electricity under private management, a process started in 2001. Potential investors are wary of the financial risks of investing in the rehabilitation of the distribution network, and little progress

	Budget	Outcome
Resources 1/	37.4	40.4
Domestic revenue	28.9	29.6
Oil 2/	18.4	20.7
Non-oil	10.5	8.9
Domestic financing	-0.3	3.0
Domestic bank credit	-0.5	0.0
Exceptional oil receipts	0.0	2.9
Privatization	0.2	0.1
World Bank support	0.0	0.4
Accumulation of external arrears	7.2	7.3
Debt relief	0.0	0.1
Financing gap	1.5	0.0
Uses 3/	37.4	40.4
Current primary expenditure and net lending 2/	14.6	17.3
Domestically financed investment	4.9	5.4
Interest charges due	5.4	5.8
Amortization due	12.3	8.3
Structural reform cost	0.0	0.4
Domestic debt and arrears payment	0.2	2.8
Large domestic suppliers	0.0	1.9
Priority arrears 4/	0.2	1.0
External arrears payment	0.0	0.3

Sources: Congolese authorities; and Fund staff estimates.

1/ Excluding foreign loans to finance investment.

2/ Includes an amount of CFAF 34 billion that was automatically transferred to the Nkossa field (in line with a 2001 agreement on the allocation of previous losses on oil exploration).

3/ Excluding foreign-financed investment.

4/ Related to salaries, pensions, and small and medium-sized enterprises.

¹ For 2003, the effect of higher prices was more than offset by lower production.

Box 4. Legal Settlement with an International Oil Company

The authorities have assured the staff that the full financial impact of the legal settlement in 2003 with an international oil company (IOC) has been properly recorded at the treasury.¹ In particular, they have assured the staff that the cash payment of US\$80 million is not an oil-collateralized loan of the government (as claimed in press reports).²

Under the agreement, the Congo's claims included grievances with respect to the

- (i) economic terms of the 1995 transition from a regime of concessions to shared production;
- (ii) price of the 1995 purchase by the IOC of the government's share of a jointly owned oil company;
- (iii) management of escrow accounts that provision for expenditures related to the abandonment and remediation of oil wells; and
- (iv) treatment of interest payments related to the repayment of oil-collateralized debt and interest earnings on the abandonment and remediation provisions.

The IOC's counterclaim centered on the government's unilateral confiscation of a previously allocated license area (which was awarded to a different private company under the production-sharing agreement for the Common Zone with Angola).

Under the reported terms of the final agreement, and in exchange for relinquishing any and all claims related to the period prior to January 1, 2003, the authorities confirmed the receipt of the following financial benefits:

- in 2003 in the form of cash, US\$80 million on account of general damages and US\$40 million on account of item (iv) above;
- in 2003, one additional shipment of crude, equivalent to approximately US\$25 million, on account of item (iii) above; and
- in the future, US\$70 million, to be paid (net of possible legal awards) upon the conclusion of a legal case brought, before European courts, by an external creditor against the Congo.

Additionally, the Congo obtained a rescheduling of payments on oil-secured loans (related to government expenditures carried out by the oil company prior to 2002), and secured the right to comanage the funds related to the abandonment and remediation provisions.

¹ A confidentiality clause, reportedly inserted at the request of the oil company, prevents the government from sharing the source documentation with staff.

² The cash payment of US\$80 million resulted from a series of transactions, namely: (i) the transfer of the operating license on an oil field (known as Likouala) by the IOC to the government; (ii) the subsequent sale of the operating license by the government to a private Congolese company; and (iii) the contracting of an oil-collateralized loan by the Congolese company to finance the US\$80 million cash payment to the government. The authorities have explained that, whereas the IOC preferred to transfer the operating license (rather than effecting a cash payment), the government did not wish to absorb the risk of operating an oil field.

has been registered. However, the bidding process for the management contract of the Pointe-Noire-Brazzaville railroad is forging ahead, with the submission of technical bids by end-2003. At odds with the government's privatization strategy, the Société Nationale Pétrolière du Congo (SNPC) embarked in 2003 on a diversification strategy, including into non-oil activities such as finance, air transport, and services, financed out of a non-oil investment budget equivalent to 0.5 percent of GDP in 2003.

IV. REPORT ON THE DISCUSSIONS

A. Medium-Term Challenges

15. **The discussions focused on how to cast economic and financial policies in a medium-term context** in order to safeguard macroeconomic stability, enhance policy credibility, and create conditions for broad-based economic growth and poverty alleviation. In this context, the staff underscored the following key medium-term challenges:

- reinforcing the framework for peace and social stability by making further progress in the participatory approach to economic reforms;
- continuing to strengthen the framework for enhanced transparency and governance in the oil sector;
- ensuring long-term fiscal sustainability in the face of uncertain future oil revenues, and avoiding procyclical public spending;
- strengthening public expenditure management and institutional capacity; and
- creating favorable conditions for private sector expansion and poverty reduction.

16. **The authorities are faced with the daunting challenge of setting the country on a path of sustainable growth and poverty reduction.** The related discussions focused on the key constraints on growth, including the heavy dependence on oil and low access to information (see Box 5 for a cross-regional comparison of Congo's performance), as well as weak institutions and poor governance (Box 6). The authorities generally concurred with this assessment and stressed that the legacy of central planning and the associated antibusiness bias, the civil conflicts, the lack of infrastructure, and the heavy debt burden were key hurdles in relaunching economic growth.

17. **There was broad agreement on the policy agenda.** In particular, the authorities concurred with the critical need for (i) improvements in governance and fiscal management, including a break from the propensity for stop-go fiscal policy, and (ii) a clear strategy to promote sustainable growth in the non-oil sector. Overall, the authorities stressed the urgency of the reconstruction effort. The staff emphasized that success in the implementation of their development plan will depend on the ability of policymakers to fully mobilize domestic resources, improve the quality of fiscal expenditures, and ensure that fiscal policy is on a sustainable path.

Box 5. Constraints on Economic Growth, 1980–99

(Period averages in units indicated)

Indicator	Congo		Low-Income Economies		Lower Middle Income Economies	
	1980s	1990s	1980s	1990s	1980s	1990s
Economic performance						
GDP per capita (constant 1995 U.S. dollars)	981	839	371	430	957	1129
GDP per capita growth (annual percent change)	3.8	-2.1	2.4	1.0	2.3	1.7
Gross domestic investment (in percent of GDP)	33	25	20	22	25	26
Fuel export (in percent of merchandise exports)	88	88	40	20	13	12
Broad money (in percent of GDP)	17	17	30	36	43	62
Cost structure/productivity						
Telephone average cost of local call (U.S. dollars per three minutes)	...	0.22	...	0.07	...	0.03
Cereal yield (kg per hectare)	792	779	1158	1236	1822	1987
Fertilizer consumption (100 grams per hectare of arable land)	120	173	406	597	1163	1146
External assistance/debt						
Aid per capita (current U.S. dollars)	51	78	9	12	5	9
External debt (in percent of GDP)	133	214	32	56	22	34
Physical infrastructure						
Irrigated land (percent of cropland)	0.5	0.5	21.1	24.3	29.4	24.2
Paved roads (in percent of total roads)	...	10	...	17	...	52
Social indicators						
Adult illiteracy rate (in percent of people age 15 and above)	42	27	50	42	25	18
Primary school enrollment ratio 1/	144	111	86	91	111	112
Secondary school enrollment ratio 2/	75	54	32	40	50	63
Immunization ratios 3/	61	50	25	60	75	90
Infant mortality rate (per 1000 live births)	86	82	103	87	49	39
Life expectancy at birth (in years)	51	51	55	58	67	68
Rural access to improved water source (fraction of rural population) 4/	...	17	...	70	...	70
Urban access to improved water source (fraction of urban population) 4/	...	71	...	90	...	95
Access to information						
Daily newspapers (per 1,000 people)	3	8	19	41	43	51
Radios (per 1,000 people)	82	116	92	142	180	317
Television sets (per 1,000 people)	3	8	21	63	66	215
Population structure						
Rural population (percent of total population)	52	40	75	71	65	59

Source: World Bank Social Indicators database; Congolese authorities; and staff estimates.

1/ In percent of the number of children of secondary school age.

2/ In percent of the number of children of secondary school age.

3/ In percent of the number of children under 12 months for immunization against diphtheria, tetanus, and polio.

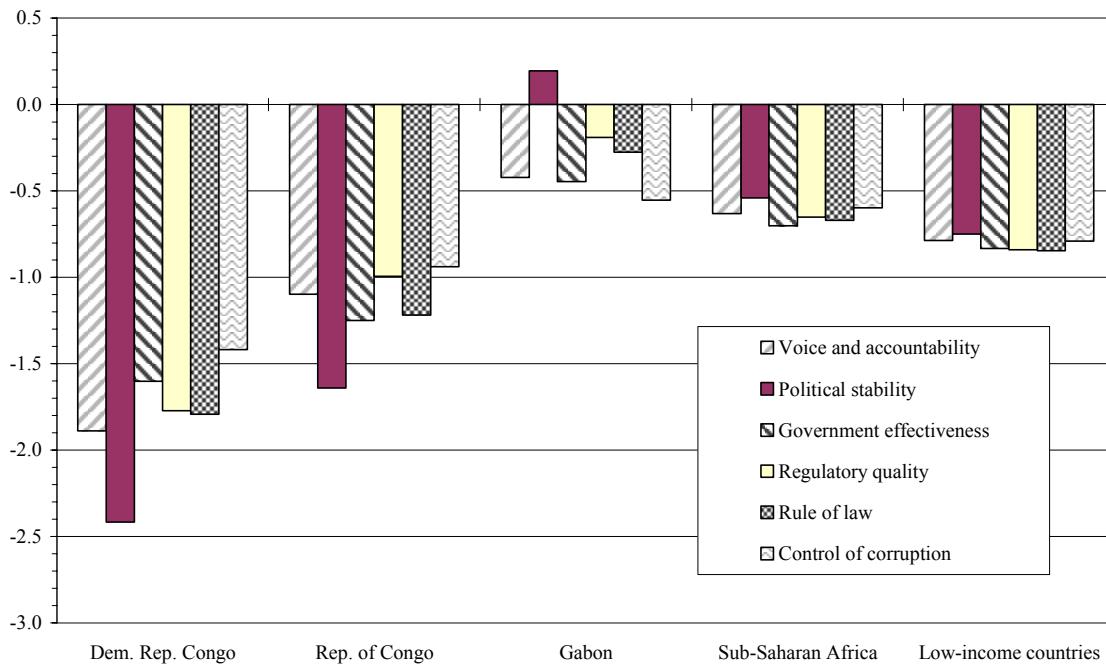
4/ Data available for 2000.

From the comparative data above, key constraints on growth and poverty reduction in the Congo appear to relate to the (i) high dependence on oil; (ii) low access to information; (iii) heavy public debt burden; (iv) high cost of public utilities; (v) low degree of financial depth; (vi) deteriorating social indicators; (vii) weak infrastructure; and (viii) urban bias. Recent research has shown that a (i) high dependence on natural resources significantly raises the probability of domestic conflicts and is inversely related to the income of the poor; and (ii) there is a strong positive relationship between the income of the poor, on the one hand, and financial depth and secondary school enrollment, on the other.

Box 6. Institutions and Governance

The legacy from past public management weaknesses and recurring bouts of civil conflict is reflected in low governance ratings (including political stability and rule of law). Using a broad definition of governance as “the traditions and institutions by which authority in a country is exercised” and combining several individual measures into clusters, World Bank researchers have constructed aggregate indicators of six dimensions of governance (www.worldbank.org/wbi/governance/wp-governance.htm). The indicators are measured in units ranging from about –2.5 to 2.5, with higher values corresponding to better governance outcomes.

Institutions and Governance: Aggregate Indicators, 2002



For economic agents, the implications of the low ratings on the quality of institutions and governance are effectively captured by assessments of the business environment carried out by COFACE (French export credit agency). According to these rankings, available at www.coface.fr, Congo is rated as “very uncertain with a poor payment record” (the second-lowest grade on a scale of 7 points) for short-term deals, and as “very high risk” (the lowest grade on a scale of 4 points) for long-term investments.

In the preparation of a national anticorruption program, the government in 2003, with assistance from the UNDP: (i) carried out a corruption survey, (ii) commissioned a study, and (iii) organized a seminar with the participation of officials, experts and representatives from civil society and the international donor community. The survey established the widespread nature of corruption in Congo: half of the 6,144 respondents reported having paid bribes to government officials. The survey also identified poverty, a lack of adequate controls, and an ineffective judicial system as the most important causes of corruption.

18. **To launch the non-oil economy, the authorities favor a strategy that emphasizes infrastructure development**, including roads to improve market access for the agricultural sector. The authorities emphasized the need to foster development in the north of the country (for which the Ollombo International Airport is being built) and to improve the delivery of basic services, especially water and electricity (for which the recently launched Imboulou Dam project is considered strategic). The staff noted that improving competitiveness in the non-oil sector will require creating a more favorable environment for private sector expansion, including through improved public service delivery and physical infrastructure, as well as an enhanced overall governance framework to effectively combat corruption (see Section IV.E).

19. **The staff stressed that, in determining the appropriate mix of development expenditures, prospective projects needed to be carefully vetted to ensure economic viability.** In particular, the limits of capacity absorption must be taken into account, and consistency with the objectives laid out in the interim poverty reduction strategy paper (I-PRSP) must be ensured. The staff also cautioned that attempts to quickly launch a number of projects aimed at the agricultural sector must take into account the currently high rate of urbanization and the tendency for people to remain in the urban area, where services are more widely available.

20. **The staff met with a wide range of stakeholders, including parliamentarians, donors, labor leaders, and civil society.** They broadly endorsed the government's efforts to improve fiscal management practices and underscored the importance of more rapid progress on the transparency front in order to ensure full mobilization of domestic resources. The role of the Bretton Woods institutions in promoting transparency was widely lauded, and there was general agreement on the importance of moving to a formal Fund-supported program and obtaining debt relief. A common theme from these meetings centered on the need for the government to broaden policy discussions and expand reform ownership.

B. Macroeconomic Outlook

21. **Real GDP is projected to grow by about 3½-4 percent per annum during 2004-07**, propelled by an annual average non-oil real GDP growth rate of about 4 percent (see Box 7 on the sources of growth). The non-oil-real GDP growth projections assume a "catch-up" factor of about ½-1 percentage point per annum, reflecting increased capacity utilization owing to the expected continued rebound in economic activity. The authorities argued that the Congo had a much higher growth potential, but the staff stressed the need for realism and analytical support for growth projections. The staff's estimates suggest that achieving the Millennium Development Goal (MDG) target of halving the proportion of the population living below the poverty line would require a non-oil real GDP growth of about 7-8 percent per year during 2004-15.

Box 7. Sources of Economic Growth, 1970–2003

A growth-accounting framework with the following production function is used for the analysis: $Y=AL^{0.6}K^{0.4}$, where: Y is real GDP; A , typically known as the Solow residual, represents total factor productivity (TFP); L is labor; and K is physical capital. The results are summarized below:

	Republic of Congo: Sources of Growth, 1970-2003 (In percentage change; unless otherwise indicated)							
	1970-74	1975-79	1980-84	1985-89	1990-94	1995-99	2000-03	1970-2003
Real GDP growth	7.8	3.2	14.3	-0.7	-0.1	1.7	4.1	4.3
Factor accumulation 1/	5.1	3.6	6.0	1.9	2.1	1.8	2.5	3.3
Solow residual	2.7	-0.4	8.3	-2.6	-2.2	-0.1	1.6	1.0
Memorandum items:								
Non-oil sector real GDP growth	3.0	4.2	14.9	-3.3	-1.7	-2.8	10.3	3.3
Oil sector real GDP growth	86.5	1.9	12.5	9.3	3.8	9.1	-4.3	17.6
Investment-GDP ratio (in percent)	29.4	30.0	42.5	22.4	28.4	29.2	23.5	29.5
Public investment-GDP ratio (in percent)	2.8	4.8	19.8	7.7	1.8	6.0	8.1	7.3
Terms of trade 2/	91.0	83.5	179.6	125.8	84.1	78.0	124.2	109.0
Real effective exchange rate 2/	108.3	109.8	96.7	98.8	92.7	79.3	80.2	95.6

Sources: Congolese authorities; and staff calculations.

1/ Accumulation of capital and labor, using 0.4 and 0.6 as factor shares, respectively.

2/ Index, 1990=100.

- Factor accumulation explained the bulk of output growth during 1970–2003, with TFP playing a limited role.
- Starting in the second half of the 1980s, the decline in non-oil real GDP growth appears to have been caused by a loss in competitiveness (due to the overvaluation of the CFA franc) and to have been accompanied by an acceleration of rural to urban migration.
- Developments in the 1990s reveal the devastating impact of civil conflicts along with indications of a “catch-up” factor, in the form of higher productivity, during the latest post-conflict period.

22. **In view of the appreciating trend in the real effective exchange rate, vigilance is required on the fiscal policy front.** In this regard, the proposed consideration by the government to adopt, starting in 2005, a fiscal rule under which oil revenues (and, consequently, expenditures) would be projected on the basis of a conservative oil price² is a welcome step. The staff noted that a key lesson from last year's budget implementation was that, for a price rule to be effective, the government would need to discuss it with the parliament and seek its endorsement, and to regularly update the parliamentarians on budgetary execution. Additionally, an enabling framework, including transparency on oil revenue and clear rules on the use of windfall revenues, would need to be in place.

23. **Given that the Congo is a member of a monetary union, sound fiscal policy is key to achieving and sustaining macroeconomic stability.** Inflation is projected to average about 2 percent annually, as domestic demand is to be held in check by fiscal prudence. The

² Calculated as the World Economic Outlook (WEO) price projection minus US\$2 per barrel.

macroeconomic projections assume an improvement in the non-oil basic primary fiscal balance (of about 5½ percentage points of non-oil GDP during 2003-07), with about 2 percentage points from non-oil revenue mobilization and the remainder from non-oil-related expenditure compression (see Table 4 below).

Table 4. Republic of Congo: Fiscal Profile, 2002-2007						
	2002 Est.	2003 Est.	2004 Proj.	2005 Proj.	2006 Proj.	2007 Proj.
(In percent of GDP)						
Domestic revenue (excluding grants)	27.2	29.6	27.3	27.5	27.3	27.2
Domestic primary expenditure 1/ 2/	26.0	22.8	21.5	23.1	23.2	23.0
Current primary expenditure	18.4	17.3	15.9	16.9	16.8	16.4
<i>Of which</i> : excluding transfers to HydroCongo 3/	16.2	15.6	15.5	16.5	16.4	16.1
Domestically-financed investment 2/	7.6	5.5	5.6	6.2	6.4	6.6
Basic primary fiscal balance	1.2	6.8	5.8	4.4	4.1	4.1
(In percent of non-oil GDP)						
Non-oil revenue	17.8	17.6	18.2	18.7	19.1	19.5
Non-oil primary expenditure	51.3	41.5	41.1	40.5	39.2	37.8
Non-oil basic primary balance	...	-23.9	-22.9	-21.8	-20.2	-18.5

Sources: Congolese authorities; and IMF staff estimates and projections.

1/ Noninterest current expenditure plus domestically financed investment.

2/ Including net lending.

3/ Excess oil revenue (which arises when operating costs of oil companies are lower than the limits stipulated in production sharing agreements) is partly assigned automatically to cover an existing liability (HydroCongo).

24. **Non-oil revenue is projected to increase by about 0.5 percent of GDP per annum.** This objective is ambitious but feasible, as the authorities have already undertaken a number of measures in 2003 (Box 2), and others are envisaged during the SMP period and over the medium term. Given that tax policy is carried out in the context of the Central African Economic and Monetary (CEMAC) region, there is limited scope for raising tax rates (with the exception of the doubling of the statistical tax to 2 percent in 2004 and its extension to oil companies). The projected increase in the non-oil revenue in later years is to be achieved from measures to widen the tax net, combat fraud and evasion, and progressively eliminate ad hoc exemptions. The authorities were of the view that there was considerable upside potential to the non-oil revenue forecast, but agreed with the staff on the need for prudence.

25. **On the expenditure side, the staff stressed that it would be critical that the share of poverty-related spending rise over time.** The projected decline in transfer payments would be expected to create room to start achieving this objective. Budgetary transfers on account of oil-related liabilities (HydroCongo) will decline on the basis of revised contractual terms that shift a larger share of the repayment burden from the government to the SNPC.³

³ The SNPC inherited the related assets of HydroCongo at the time of its creation.

Transfers to the national oil refinery (CORAFA) are projected to fall on the basis of a performance contract, signed in December 2003, for the payment of crude oil deliveries.

26. Transfers to CORAF and price subsidies on consumer petroleum products are to be explicitly incorporated into the budget. The staff noted the need for early implementation of an automatic price adjustment mechanism for refined petroleum products, accompanied by appropriate safeguards to shield the poor. The authorities have decided, for the time being, to maintain the current retail prices for petroleum products, in light of the failure, amid popular dissatisfaction, to put in place a system of automatic price adjustment in October 2002. In addition, the government would need to develop a strategy for reforming CORAF so that over the medium term it can operate without recourse to fiscal subsidies.

27. The authorities agreed that the investment budget should focus on projects required to accelerate growth and poverty reduction. It will be critical that the execution of the investment budget be closely monitored in order to ensure consistency with approved outlays. In this connection, the staff stressed the importance of finalizing the work on establishing a comprehensive functional classification system. The staff also noted that public investment plans needed to give due consideration to the public resources invested by the SNPC, part of which was allocated to support the company's diversification policy. On the latter, the staff urged the authorities to prepare an action plan to have the SNPC focus on its core activities.

28. The fiscal compression over the medium term would help to generate funds to ensure external debt service.⁴ In order to allow increased spending on poverty-related outlays, the authorities stressed the need for debt alleviation. A preliminary analysis of the Congo's public debt indicates that, even after the application of full traditional Naples terms rescheduling, Congo's debt burden would remain unsustainable; the net present value (NPV) of debt-to-government revenue ratio would remain higher than 250 percent over the medium term (Appendix IV).

29. The staff noted that domestic payment arrears should be settled in an equitable and transparent manner. All domestic payment arrears of a commercial nature, as of end-2002, have been audited, and the government plans to follow up with an audit of arrears on wages and pensions.⁵ The authorities were urged to prepare a comprehensive domestic arrears settlement plan, and to publish the related policy framework. The implementation of this plan should follow budgetary procedures and be contingent on the availability of financial resources.

⁴ To multilateral institutions, Paris Club creditors on post-cutoff-date debt, and on oil-collateralized debt.

⁵ The total domestic debt stock is estimated at about 27 percent of GDP, the bulk of which represents arrears.

C. Economic Program for 2004

30. **The authorities noted that their overarching objective was to set the economy on a sustained path of growth and poverty reduction in the context of an arrangement under the PRGF.** To assist the Congo in establishing the track record necessary for moving to a PRGF-supported program, the government is implementing a new SMP covering the period January-June 2004.⁶ The primary objectives of the new SMP—which is dovetailed into the framework of a medium-term program—are to strengthen fiscal discipline and enhance oil sector transparency.

31. **A key objective of fiscal policy in 2004 is to entrench discipline in public finance management.** On the revenue side, full mobilization of domestic receipts will be facilitated by the continued certification of oil revenue by an independent auditor. In addition, non-oil revenue measures will focus on a better identification and tracking of taxpayers, modernization of the computer system at customs, and establishment of electronic links among revenue departments. The program will incorporate an adjustor to account for deviations of oil revenues from programmed amounts.⁷

32. **As regards the forestry sector,** the authorities explained that operators had resisted the increase in tax rates in 2003. The sector reform recommended by the World Bank, while calling for a gradual increase in tax rates to levels comparable to those in neighboring countries, had also envisaged a change of the tax base from “free on board” to “free on truck,” so as to exclude transport costs from the base. The authorities have yet to change the tax base under the new regime. Recognizing the fiscal burden on the sector, the government has delayed the second round of tax increases, originally planned for 2004. The staff noted that the forestry sector held good promise for economic diversification and poverty reduction. It therefore urged the authorities to carry out, with assistance from the World Bank and sector operators, a comprehensive evaluation of reform implementation.

33. **Expenditure policy is geared to raising poverty-related outlays while keeping nonproductive transfers to a strict minimum.** In 2004, traditional transfer payments are projected to increase considerably, owing to the establishment of new institutions in support of democratization, including the Audit Office, the High Court of Justice, the National Commission on Human Rights, and the Economic and Social Council. Overall, the structure of spending should gradually shift toward priority social spending.

34. **To meet pressing social needs, the government signed with the labor unions a “social truce,” whereby the gradual payment of wage and retirement pension arrears**

⁶ See the authorities’ letter of intent (Appendix III).

⁷ The basic primary fiscal balance will be adjusted upward if oil revenue is higher than projected, and the extra resources would be utilized to finance the residual budgetary gap and reduce external payment arrears on debt not eligible for rescheduling.

will begin in 2004. To this end, the 2004 budget law provides about 1.8 percent of GDP for the payment of social arrears (on wages and pensions) and priority arrears (to small and medium-sized enterprises), with a view to bolstering economic activity.

35. The structural measures for 2004 focus on oil sector transparency and public finance. In addition to increasing the level of publicly available information, the process of conducting annual external audits of the SNPC and the quarterly certification of oil revenue will continue. The 2003 accounts of the CORAF are to be audited, and a preliminary action plan to have the SNPC focus on its core activities is to be prepared. In addition, for the SNPC, it is critical that the action plan resulting from the 1999–2001 audit be quickly implemented, and that its reporting obligations to the Ministry of Finance be effectively executed. In the area of public finance, the key objectives are to ensure full revenue centralization and enhance expenditure control.

D. Monetary and Financial Sector Issues

36. Monetary and credit policies are conducted by the Bank of Central African States (BEAC) in the regional context of the CEMAC. Broad money in the Congo is expected to grow in line with domestic nominal non-oil GDP over the medium term. Net credit to the government is projected to increase in 2004 (by about 0.6 percent of GDP), but the monetary program leaves room for credit to the economy to expand and for the central bank to build up its net foreign assets.

37. Given the fragile health of the banking system, the staff is encouraged by the privatization of the remaining publicly owned bank (CAIC). As a further confidence-building measure for the banking system, and with the ultimate goal of improving access to banking services, the staff encouraged the authorities to begin addressing weaknesses in the legal and judicial system (namely, an ineffective bankruptcy law and the lack of a functional land title system) and to adopt a comprehensive plan to restructure the nonbank financial sector, with the assistance of the World Bank. In addition, the staff encouraged the authorities to steadfastly implement the proposed modernization of the payment and settlement system.

38. The authorities agreed with the need to promote the healthy development of microfinance institutions, which have offered a viable banking option for small businesses and low-income workers. Accordingly, mutual microfinance firms (MUCODEC) will continue to benefit from their tax-exempt status,⁸ and the authorities have launched a series

⁸ New regional regulations establish two main categories of microfinance institutions, with category 1 encompassing those that deal exclusively with members (such as mutuals) and category 2 including those that also lend to nonmembers and that are typically limited-liability companies. Owing to their particular role in extending credit to low-income consumers, category 1 institutions benefit from tax exemptions in many countries. There are

(continued)

of seminars to assist the sector in complying with the new regional regulations over the coming three years.

E. Transparency and Governance

39. **The authorities agreed with the importance of reinforcing recent efforts to enhance transparency and governance in the oil sector.** As part of the transparency initiative in the Congo, the staff encouraged them to consider participation in the Extractive Industries Transparency Initiative (EITI). The authorities argued that, for the time being, they would prefer to focus on the oil sector transparency measures in the 2004 SMP.

40. **The staff discussed with the authorities their action plan for addressing the weaknesses in accounting practices and fiscal agency accountability pointed out by the 1999–2001 audit of the SNPC.** It commended them for publishing, on the Internet, parts of the audit report, the SNPC action plan, and the full reports on the 2003 oil revenue reconciliation conducted by an external auditor (see www.congo-site.cg). It encouraged the authorities to move swiftly with the external audit of the SNPC's 2002 accounts, and to draw lessons from the 2003 certification of oil revenue, so as to maximize the government's take from the oil it receives as fiscal payment.

41. **To begin to tackle other aspects of governance** (Box 6), the government has (i) started preparing, with assistance from the United Nations Development Program (UNDP), a national anticorruption program, and (ii) enacted a code of conduct for civil servants and the enabling regulations for the related disciplinary councils. Additionally, in January 2004, the establishment of a National Anti-Corruption and Anti-Fraud Commission was proposed to the Council of Ministers. Under the chairmanship of the President of the Republic, this commission would monitor the implementation of anticorruption policies, centralize all information necessary for the prevention and detection of corruption, oversee procurement policy, alert competent authorities to cases of serious corruption, and assist government agencies or enterprises in tackling corruption.

F. Poverty Reduction

42. **A draft interim poverty reduction strategy paper (I-PRSP) is at an advanced stage of preparation.** It has benefited from comments from the international community, which has stressed that the document needs to do the following: (i) take a strategic approach and prioritize objectives; (ii) discuss the importance of good governance in the management of oil wealth and public finance; and (iii) present a macroeconomic framework that ascertains that the maximum domestic revenue is being mobilized and that expenditures are being oriented toward the priority sectors. Additionally, the staff stressed the importance of rapidly completing the work started in late 2003, with technical assistance from the Fund, to

efforts under way, with the support of the World Bank, to ensure that such treatment is made universal throughout the CEMAC region.

implement a functional classification system to help monitor poverty-related budgetary outlays.

G. Statistics and Technical Assistance

43. **The authorities are making efforts to improve the statistical apparatus.** The recent decisions to participate in the IMF's General Data Dissemination System (IMF Press Release No. 03/229) and to increase the resources allocated to statistical development should help ensure that this process is sustained. The data provided by the authorities and the BEAC are broadly adequate to monitor macroeconomic developments, although improvements would be needed, *inter alia*, in the coverage of the oil sector data. With a view to strengthening the poverty-related database, a number of surveys are to be launched with assistance from the World Bank and UNDP, including a household survey and a population census. Given its vast capacity-building needs, the Congo is expected to request further technical assistance from the international community, especially in the areas of public expenditure management, non-oil revenue mobilization, oil sector transparency, public debt management, and statistics.

V. FINANCING GAP, CAPACITY TO PAY, AND EXTERNAL DEBT

44. **A large core residual financing gap⁹ of about CFAF 110 billion (5.2 percent of GDP) remains in 2004-05** (Table 5 below), despite the authorities' efforts to mobilize revenues and control primary expenditures (Section IV.B; Table 4 above; and Table 12). The hump in the residual financing gap in 2005 is due primarily to the high debt service on oil-collateralized loans (CFAF 83 billion, about 4 percent of GDP). The staff advised the authorities that it may be necessary to refinance part of this debt in order to generate some room for the settlement of arrears to multilateral institutions and on post-cutoff-date debt to Paris Club creditors.

⁹ After taking into account the need to remain current on debt service due to (i) Paris Club creditors on post-cutoff-date debt, (ii) multilateral institutions, and (iii) creditors of oil-collateralized loans, but before accounting for the settlement of external payment arrears owed to (i) Paris Club creditors (on pre- and post-cutoff date debt), (ii) multilateral institutions, and (iii) commercial banks and other creditors.

Table 5. Republic of Congo: Elements of the Capacity to Pay External Debt, 2003-07 (In billions of CFA francs, unless otherwise indicated)					
	2003 Est.	2004 Proj.	2005 Proj.	2006 Proj.	2007 Proj.
Basic primary fiscal balance 1/	139.1	125.2	92.4	89.1	93.8
Core debt service due 2/	-111.1	-128.5	-151.2	-72.0	-67.9
Identified financing	36.5	11.4	-3.0	-3.0	-3.0
Identified arrears payments 3/	-64.6	-38.3	-15.0	-15.0	-15.0
Residual balance	0.0	-30.2	-76.2	0.2	9.7
Memorandum items:					
Arrears on core external debt	384.3	...	...	...	...
Multilateral	102.7	...	...	...	...
Paris Club (post-cutoff date)	281.6	...	...	...	...
Oil-collateralized debt stock	220.7	170.9	88.1	75.2	64.2
Potential windfall oil revenue 4/	0.0	10.0	27.4	28.1	28.9
Domestically financed investment (in percent of GDP)	5.4	5.6	6.2	6.4	6.6
Primary current expenditures (in percent of GDP)	17.3	15.9	16.9	16.8	16.4
Of which: transfers	6.4	4.7	5.0	4.8	4.5
Non-oil basic primary fiscal balance (in percent of non-oil GDP)	-23.9	-22.9	-21.8	-20.2	-18.5

Sources: Congolese authorities; and Fund staff estimates and projections.

1/ Domestic revenue (excl. grants) minus expenditures (excl. foreign-financed investment and interest payments due).

2/ Due to (i) Paris Club creditors on post-cutoff-date debt, (ii) multilateral creditors, (iii) creditors of oil-collateralized loans, and (iv) domestic debt. Excludes potential impact of Paris Club rescheduling.

3/ From 2004 onward, relates to arrears payments on salaries and pensions, and small and medium-sized enterprises.

4/ Additional revenues if WEO price projections are realized; budgetary projections use conservative oil prices.

45. The scope for generating additional domestic savings to cover the residual financing gap and make external arrears payments appears limited. The authorities agreed that a settlement plan on arrears (amounting to about 19 percent of GDP; see Table 5) to multilateral institutions and Paris Club creditors (on post-cutoff-date debt) that was satisfactory to the creditors would be needed to secure financing assurances for a successor PRGF-supported program.

VI. REGIONAL INTEGRATION AND TRADE REGIME

46. Regional economic policy, led by the CEMAC, has been focused on (i) promotion of macroeconomic discipline; (ii) creation of an integrated regional financial system; and (iii) integration of regional and international goods markets. On macroeconomic discipline, which is monitored by compliance with four regional convergence criteria by end-

Table 6. Congo: Compliance with Regional Convergence Criteria, 2002-03 (In percent)			
	2002 Est.	2003 Est.	Status
Basic fiscal balance-GDP ratio (criterion: nonnegative) 1/	-7.1	1.1	Respected
Consumer price inflation (criterion: not higher than 3 percent)	3.8	1.6	Respected
Public debt-GDP ratio (criterion: not higher than 70 percent)	179.1	184.7	Not respected
Net change in government arrears-GDP ratio (criterion: nonpositive)	9.8	6.1	Not respected

Sources: Congolese authorities; and staff calculations.

1/ Overall budget balance, excluding grants and foreign-financed investment.

2003, the Congo reported good progress with two criteria met (see Table 6). On the integration of goods markets, the Congo promulgated the CEMAC's investment charter and issued two implementing regulations; and the National Law of Investment is expected to be revised, in compliance with the CEMAC charter, by end-2004. The Congo is also in broad compliance with the implementation of the regional customs code. Finally, the Congo has established the national financial intelligence unit that will implement and coordinate regional efforts to combat money laundering and the financing of terrorism.

47. **The trade and payment system is largely free of restrictions.** The Fund index of trade restrictiveness is estimated at 3 (on a scale of 1-10, where 1 is the least restrictive), with a simple average tariff rate of 16 percent and no significant nontariff barriers. With respect to the payment system, the authorities eliminated in 2003 the preclearance procedure (whereby economic operators had to receive clearance by a unit in the Ministry of Finance before submitting a request for external transfers to a commercial bank); the Congo is now in compliance with the CEMAC harmonized foreign exchange arrangement. However, temporary controls imposed by the BEAC on external transfers have generated concerns on the part of operators (Box 3). These controls are expected to be eased as the external coverage ratio rises above the minimum threshold established by the BEAC.

VII. RISKS

48. **Despite the recent success in consolidating peace, the Congo continues to face risks to the continuance of sound economic performance.** To maintain the reform momentum, there is a pressing need to broaden the policy discussions and expand ownership of the reform process. Key challenges for economic policy include the growing pressures for "peace dividends" (in the form of higher public expenditures), management of oil price volatility, and the need to curtail the impact of special interests. In addition, it will be critical for the national oil company to fully contribute to ongoing efforts to improve transparency and accountability in the oil sector. Finally, the timely provision of information, especially on oil-related activities, will help to convince development partners that domestic resources are being fully mobilized.

VIII. STAFF APPRAISAL

49. **Recent developments on the political front are encouraging against the background of the recurrent conflicts in the 1990s.** Under the umbrella of peace, Congo completed a four-year political transition period, held democratic elections, and installed the full complement of democratic institutions required by the Constitution. To ensure that this period of political stability is prolonged, it is now critical to secure social stability by promptly implementing the proposed demobilization program for former combatants and tackling the huge socioeconomic challenges facing the nation. In this context, entrenching democratic institutions and installing transparent decision-making practices would effectively broaden policy discussions and expand ownership of the reform process.

50. **Accompanying the positive momentum on the political front, economic activity in the non-oil sector has picked up significantly and inflation has decelerated in the post-conflict period.** In an encouraging sign of a pickup in non-oil sector activity, credit to the economy grew in 2003 at a faster rate than non-oil GDP for the first time in three years. Nonetheless, key social indicators have deteriorated, and the external debt burden is heavy. The proportion of the population living below the poverty line increased sharply during the conflict period. Under plausible assumptions, real GDP growth is projected in the range of 3½-4 percent per year during 2004-07, which is about half of the staff's estimate of the level that would be required to lower the income poverty rate by half by 2015.

51. **Building on the momentum generated by the improvements on the political and the economic fronts, the government has begun to focus on economic management.**

Measures to enhance budget management and oil sector transparency, along with efforts at initiating a wider policy debate, augur well for the prospects of increased public support for reforms. In the period ahead, it will be critical for the government to strengthen this fledgling participatory approach to economic policy formulation. The staff urges the authorities to finalize the preparation of the I-PRSP, as it will serve as a key ingredient for the international community's support for the country in the period ahead. The I-PRSP should provide a road map for the policies required to accelerate non-oil sector growth, manage oil sector resources effectively, and reduce poverty. To help monitor poverty-related outlays, it is critical that the implementation of a comprehensive functional classification system for the budget be completed promptly.

52. **Performance in 2003, in the context of the implementation of the SMP for that year, was weak and did not allow Congo to move to a PRGF-supported program.** While some encouraging results were observed, notably on oil sector transparency, the achievements were outweighed by the unbudgeted use of windfall oil revenue, the underperformance in non-oil revenue, and weaknesses on the part of the national oil company in carrying out its fiscal agency role. In the period ahead, the authorities will need to remain vigilant with respect to fiscal discipline and bold in tackling the influence of vested interests.

53. **The staff regrets the opportunity missed in 2003 by not using additional oil revenues to clear a significant amount of external arrears.** The choice made by the Congo to clear domestic commercial arrears contributed not only to weak program implementation, but also to a setback to the authorities' goal of moving quickly to a PRGF-supported program and securing the goodwill of the international community. The staff urges the authorities to use future additional oil revenues in accordance with stated program priorities.

54. **The staff is encouraged by the authorities' renewed determination to strengthen the framework for moving to a medium-term program for growth and poverty reduction that can be supported by the international community.** The program for 2004 appropriately addresses the most pressing issues facing the Congo, and the authorities are encouraged to diligently implement the proposed measures. The authorities are cognizant, however, that obtaining financing assurances for a Fund-supported medium-term program

would entail receiving exceptionally favorable treatment on post-cutoff-date arrears to the Paris Club and arrears to multilateral creditors. The international community, in turn, will need assurances from the government that it is making the maximum effort to implement reforms, and to mobilize domestic resources and utilize them judiciously.

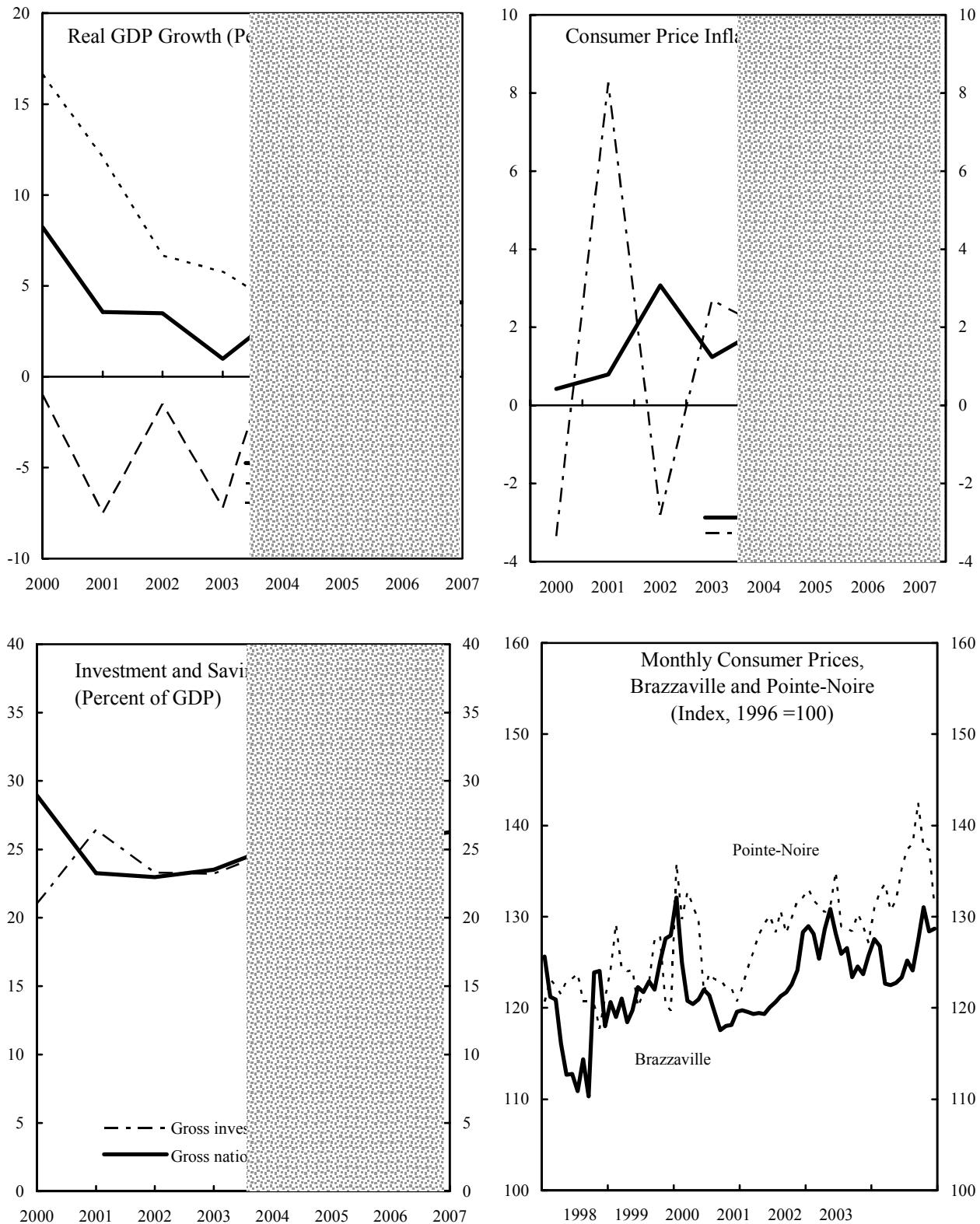
55. The Congo is faced with daunting challenges in moving onto a sustainable path of economic development. Increased focus on oil sector transparency and governance, together with access by the public to information on economic management, should be key aspects of a strategy to lower the probability of future conflicts and to strengthen the decision-making process. In addition, actions to ensure that oil-related resources are being fully accounted for will be key to strengthening domestic ownership and securing the exceptional donor support that the Congo needs to move to a PRGF-supported program. Another key challenge will be to improve the business climate by enhancing, *inter alia*, the overall governance framework and effectively combating corruption, and by improving efficiency in the delivery of public utilities.

56. While the real effective exchange rate remains below its pre-1994 devaluation level, vigilance is required on fiscal policy in view of the strengthening of the euro and the rise in the terms of trade. In this regard, the staff is encouraged by the authorities' stated objective to adopt a fiscal rule, starting in 2005, to project oil revenues and to program expenditures on the basis of a conservative price assumption. In addition, with a view to enhancing the Congo's non-oil sector competitiveness, the staff urges the authorities to work in concert with development partners to tackle the fundamental causes of the high cost of doing business in the Congo.

57. The timely provision of reliable economic and financial data is essential for effective macroeconomic management and Fund surveillance. The provision of comprehensive information, including on oil-related activities, will help to convince development partners that domestic resources are being fully mobilized.

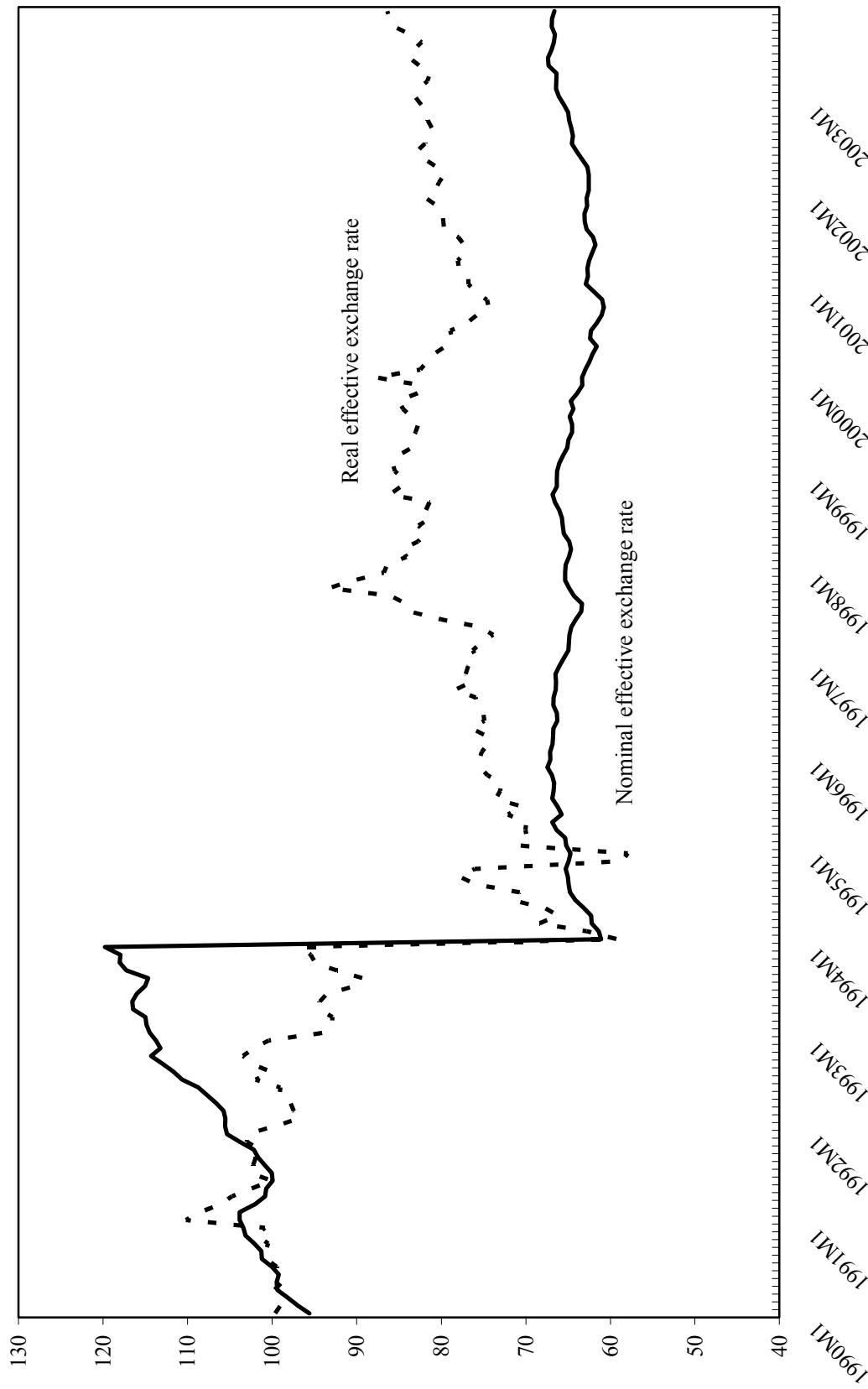
58. The staff proposes that the next Article IV consultation be held on the standard 12-month consultation cycle.

Figure 1. Republic of Congo: Economic Activity and Prices, 2000–07



Sources: Congolese authorities; and staff estimates.

Figure 2. Republic of Congo: Effective Exchange Rates, January 1990–December 2003
(Index, 1990 = 100)



Source: IMF, Information Notice System.

Table 7. Republic of Congo: Selected Economic and Financial Indicators, 2000–07

	2000	2001	2002	2003	2004	2005	2006	2007
			Est.	Init. Proj.	Est.		Projections	
(Annual percentage change)								
Production and prices								
GDP at constant prices	8.2	3.6	3.5	2.0	1.0	3.6	3.7	4.0
Oil	-1.0	-7.5	-1.5	-5.5	-7.2	3.2	2.8	2.8
Non-oil	16.6	12.1	6.7	6.4	5.8	3.8	4.1	4.6
GDP at current prices	58.2	-10.9	2.9	-6.2	-3.0	5.2	-2.0	3.3
GDP deflator	46.1	-13.9	-0.6	-8.0	-3.9	1.5	-5.5	-0.6
Consumer prices (period average)	0.4	0.8	3.1	2.0	1.2	2.0	2.0	2.0
External sector								
Exports, f.o.b. (CFA francs)	82.0	-13.6	4.0	-22.0	-5.9	-1.4	-6.5	0.3
Imports, f.o.b. (CFA francs)	31.8	17.8	-1.5	2.3	-4.2	5.9	1.9	5.2
Export volume	7.2	8.9	5.8	4.8	-4.7	9.1	2.2	3.5
Import volume	17.3	17.0	-0.7	4.5	1.7	9.7	3.1	5.0
Terms of trade (deterioration -)	51.0	-13.6	3.7	-23.4	2.0	-4.8	-9.1	-3.3
Nominal effective exchange rate	-4.5	1.0	2.1	...	4.3	...	...	...
Real effective exchange rate	-5.9	-0.4	3.5	...	6.1	...	...	...
Central government finances								
Total revenue	56.0	3.7	-8.9	6.1	6.6	-1.6	-1.4	2.8
Oil revenue	69.1	-7.6	-7.7	-5.7	6.1	-8.5	-7.1	-1.8
Non-oil revenue	25.5	44.7	-11.7	23.2	4.4	9.9	9.3	10.2
Total expenditure	22.7	10.7	15.3	-24.0	-18.7	21.6	2.6	3.3
Current	9.8	30.4	27.8	-27.6	-16.4	18.9	1.4	2.4
Capital	78.9	28.8	-11.5	-12.8	-25.8	31.0	6.2	5.9
(In percent of beginning-of-period broad money, unless otherwise indicated)								
Money and credit								
Net domestic assets	-11.1	14.5	8.8	-1.2	8.5	5.8	0.8	1.2
Domestic credit	-8.9	3.0	-6.8	-1.2	5.2	5.8	0.8	1.2
Central government	-6.6	21.0	9.0	-3.4	0.4	4.0	-1.0	-0.9
Credit to the economy	-4.5	-16.4	-16.5	2.1	5.3	1.8	1.8	2.2
Broad money	58.5	-22.8	13.1	8.6	-2.4	6.3	6.4	7.7
Velocity of broad money (non-oil)	2.9	3.0	3.6	3.4	3.6	3.6	3.6	3.6
(In percent of GDP)								
Investment and saving 1/								
Gross national saving	29.0	23.3	23.0	22.5	23.5	19.6	18.9	18.9
Gross investment	21.0	26.4	23.3	25.8	23.2	24.8	25.3	25.4
Central government finances								
Revenue and grants	26.6	30.9	27.4	29.0	30.1	28.1	28.3	28.2
Total expenditure	25.5	31.6	35.4	26.9	29.7	34.3	35.9	35.9
Of which: exceptional interest 2/	...	...	...	...	...	5.6	6.4	6.8
Overall balance (deficit -, commitment) 3/	1.1	-0.7	-8.1	2.1	0.4	-0.6	-1.2	-1.0
Primary balance (deficit -) 4/	8.4	6.8	1.2	9.3	6.8	5.8	4.4	4.1
Of which: non-oil primary balance	-11.9	-14.3	-15.6	-9.0	-12.2	-11.8	-12.2	-11.7
Current account balance 5/	7.9	-3.2	-0.3	-3.3	0.3	0.3	-0.1	0.2
External public debt (end of period)	163.2	196.3	179.1	203.5	184.7	181.3	189.9	192.6
(In percent of exports of goods and services)								
External public debt service (before debt relief)	24.0	23.2	22.9	25.8	16.8	24.2	26.9	21.9
External public debt	203.3	245.1	222.1	294.9	234.3	243.8	264.9	275.0
(In percent of total government revenue excluding grants)								
External public debt service (before debt relief)	73.4	60.4	68.0	59.5	44.7	66.0	70.3	56.1
External public debt	621.0	638.4	658.9	680.1	624.1	664.3	691.9	705.3
(In billions of CFA francs, unless otherwise indicated)								
Gross official foreign reserves	158.6	53.6	22.2	46.4	20.5	18.7	27.9	45.7
In months of imports, c.i.f.	4.5	1.3	0.5	1.1	0.5	0.4	0.7	1.0
Nominal GDP	2,293	2,043	2,103	2,047	2,040	2,146	2,102	2,172
World oil price (U.S. dollars per barrel) 6/	28.2	24.3	25.0	22.0	29.0	28.7	25.0	24.0
Oil production (in millions of barrels)	96.8	89.6	88.0	82.0	81.7	84.3	86.7	89.1
Potential windfall oil revenue 7/	...	...	...	...	...	...	27.4	28.1

Sources: Congolese authorities; and staff estimates and projections.

1/ Saving and investment data are preliminary. Balance of payments estimates are being revised with Fund technical assistance.

2/ Interest due on external arrears and residual financing gap.

3/ Including grants, excluding interest due on external arrears and residual financing gap.

4/ Revenue minus noninterest current expenditure minus domestically financed capital expenditure.

5/ Including public transfers, and excluding interest due on external arrears and residual financing gap.

6/ From 2005 onward, WEO price forecasts are reduced by US\$2 per barrel (see note 7 on price rule).

7/ Following a price rule, oil revenue from 2005 onward is projected on the basis of an international price estimated to be US\$2 lower than the latest WEO forecasts. Alternatively, using WEO price forecasts would increase oil revenue and generate windfall oil revenues.

Table 8. Republic of Congo: Central Government Operations, 2000–07

	2000	2001	2002	2003		2004	2005	2006	2007
				Init. Proj.	Est.			Projections	
(In billions of CFA francs)									
Revenue and grants	609.4	631.8	575.4	610.5	613.5	603.6	595.4	611.8	636.8
Revenue	602.6	628.1	571.7	589.8	603.6	585.6	577.1	593.1	617.7
Oil revenue	466.2	430.8	397.5	375.0	421.6	385.6	358.4	352.0	353.4
Non-oil revenue	136.4	197.3	174.2	214.8	182.0	200.0	218.7	241.1	264.3
Grants	6.8	3.7	3.7	20.7	9.9	18.0	18.4	18.7	19.1
Expenditure and net lending	583.5	645.9	746.4	566.7	606.1	736.2	755.1	779.8	807.8
Current expenditure	424.1	440.6	563.1	407.6	470.5	559.6	567.5	581.1	597.8
Wages	106.7	118.1	120.4	120.0	120.2	124.5	127.0	129.5	132.1
Other current expenditure	156.1	159.8	256.7	162.2	223.6	200.6	210.7	215.4	222.7
Material and supplies	36.7	32.1	78.4	50.0	50.0	51.8	54.1	58.2	62.7
Common charges	72.4	55.0	73.4	42.8	42.8	47.9	50.0	52.8	55.8
Transfers	47.0	72.7	104.9	69.4	130.8	100.9	106.6	104.5	104.2
Filière carburants	...	...	6.9	1.8	12.5	7.0	8.0	5.0	5.0
HydroCongo	...	...	44.8	0.0	33.0	8.0	10.0	8.0	8.0
CORAF	...	...	...	...	16.0	8.0	6.0	4.0	0.0
Other transfers	47.0	72.7	53.2	67.6	72.2	77.9	82.6	87.5	91.2
Local authorities	2.4	10.7	9.3	16.0	8.9	15.2	17.0	19.0	19.0
Interest	158.9	152.0	176.7	109.3	117.8	219.3	212.9	217.1	224.0
Domestic	9.7	7.7	14.4	13.5	23.4	14.8	12.3	10.7	11.8
External	149.2	144.3	162.3	95.8	94.4	204.5	200.5	206.4	212.2
Capital expenditure	159.4	205.4	181.7	158.5	134.8	176.6	187.6	198.8	210.0
Domestically financed	144.6	200.4	158.1	100.4	111.0	120.1	130.0	140.0	150.0
Externally financed	14.8	5.0	23.6	58.1	23.8	56.5	57.6	58.8	60.0
Net lending	0.0	0.0	1.6	0.6	0.8	0.0	0.0	0.0	0.0
Primary balance 1/	192.8	139.2	25.7	190.5	139.1	125.2	92.4	89.1	93.8
<i>Of which: non-oil primary balance</i>	-273.4	-291.7	-327.0	-184.5	-248.2	-252.4	-255.9	-254.9	-251.6
Balance, commitment basis									
Excluding grants	19.1	-17.8	-174.6	23.1	-2.5	-150.6	-178.1	-186.7	-190.1
Including grants	25.9	-14.1	-171.0	43.8	7.4	-132.6	-159.7	-168.0	-171.0
<i>Of which: non-oil balance</i>	-440.3	-444.9	-523.7	-331.2	-379.9	-510.2	-508.1	-512.0	-516.4
Change in arrears	268.2	73.6	205.9	147.2	124.8	236.9	253.3	261.5	252.0
External	283.4	104.5	210.8	147.2	164.2	266.4	268.3	276.5	267.0
Domestic	-15.2	-30.9	-5.0	0.0	-39.5	-29.5	-15.0	-15.0	-15.0
Balance, cash basis	294.1	59.5	34.9	191.0	132.2	104.3	93.6	93.5	81.0
Financing	-294.0	-59.5	-34.9	-222.7	-132.1	-134.4	-171.6	-96.8	-80.5
Foreign (net)	-239.4	-85.0	-15.0	-212.8	-146.1	-137.0	-158.2	-83.3	-67.1
Drawings	44.0	73.4	234.1	37.4	21.6	38.5	39.3	40.1	40.9
Amortization due	-292.7	-233.6	-259.7	-250.2	-169.3	-175.5	-197.4	-123.3	-107.9
Rescheduling obtained	2.8	11.6	4.3	0.0	1.5	...	...	...	...
Domestic (net)	-54.6	25.5	-19.9	-9.9	14.0	2.6	-13.5	-13.5	-13.5
Banking system (net)	-13.9	75.1	23.2	-9.8	1.0	11.4	-3.0	-3.0	-3.0
Nonbank financing	-40.7	-49.5	-43.1	-0.1	13.0	-8.8	-10.5	-10.5	-10.5
Sale of assets	3.1	3.0	7.5	4.4	2.1	1.9	0.0	0.0	0.0
Cost of financial sector reforms	-18.7	-20.9	-3.8	0.0	-0.6	0.0	0.0	0.0	0.0
Cost of structural reforms	-9.2	-1.2	-7.6	0.0	-7.6	-1.9	0.0	0.0	0.0
Exceptional oil receipts	0.0	0.0	0.0	0.0	59.2	0.0	0.0	0.0	0.0
Domestic debt and other	-15.9	-9.3	-16.9	-4.5	-40.1	-8.8	-10.5	-10.5	-10.5
Statistical float	0.0	-21.1	-22.3	0.0	0.0	0.0	0.0	0.0	0.0
Financing gap	0.0	0.0	0.0	31.7	0.0	30.2	78.0	3.3	-0.5

Table 8. Republic of Congo: Central Government Operations, 2000–07 (concluded)

	2000	2001	2002	2003		2004	2005	2006	2007
				Init. Proj.	Est.				Projections
(In percent of GDP)									
Revenue and grants	26.6	30.9	27.4	29.0	30.1	28.1	28.3	28.2	28.0
Revenue	26.3	30.7	27.2	28.0	29.6	27.3	27.5	27.3	27.2
Oil revenue	20.3	21.1	18.9	17.8	20.7	18.0	17.0	16.2	15.5
Non-oil revenue	5.9	9.7	8.3	10.2	8.9	9.3	10.4	11.1	11.6
Total expenditure	25.5	31.6	35.4	26.9	29.7	34.3	35.9	35.9	35.5
Primary expenditure	17.9	23.9	26.0	19.0	22.8	21.5	23.1	23.2	23.0
Current	11.6	14.1	18.4	14.2	17.3	15.9	16.9	16.8	16.4
Wages	4.7	5.8	5.7	5.7	5.9	5.8	6.0	6.0	5.8
Other	6.9	8.3	12.6	8.5	11.4	10.1	10.8	10.8	10.6
Capital and net lending	6.3	9.8	7.6	4.8	5.5	5.6	6.2	6.4	6.6
Interest	6.9	7.4	8.4	5.2	5.8	10.2	10.1	10.0	9.9
Foreign-financed capital expenditure	0.6	0.2	1.1	2.8	1.2	2.6	2.7	2.7	2.6
Overall balance, commitment basis 2/	1.1	-0.7	-8.1	2.1	0.4	-6.2	-7.6	-7.7	-7.5
Excluding exceptional interest 3/	1.1	-0.7	-8.1	2.1	0.4	-0.6	-1.2	-1.0	-0.4
Primary balance	8.4	6.8	1.2	9.3	6.8	5.8	4.4	4.1	4.1
Of which: non-oil primary balance	-11.9	-14.3	-15.6	9.0	-12.2	-11.8	-12.2	-11.7	-11.1
(In percent of non-oil GDP)									
Non-oil revenue	17.3	22.3	17.8	22.0	17.6	18.2	18.7	19.1	19.5
Wages	13.5	13.3	12.3	11.5	11.6	11.3	10.8	10.3	9.7
Non-oil primary balance	-34.6	-33.0	-33.5	-17.6	-23.9	-22.9	-21.8	-20.2	-18.5
Memorandum items:									
(In billions of CFA francs, unless noted otherwise)									
Potential windfall oil revenue 4/	...	...	...	...	...	...	27.4	28.1	28.9
GDP at current market prices	2,292.5	2,043.4	2,103.0	2,047.0	2,040.0	2,145.6	2,102.1	2,172.4	2,272.7
Non-oil GDP at market prices	790.2	884.8	976.6	1,046.0	1,036.6	1,101.7	1,172.3	1,261.2	1,358.7
External debt service due 5/	149.2	198.2	200.5	198.9	87.7	113.6	128.4	50.9	45.6

Sources: Ministry of Economy, Finance, and the Budget; and Fund staff estimates and projections.

1/ Revenue minus noninterest current expenditure minus domestically financed capital expenditure and net lending.

2/ Including grants.

3/ Interest due on external arrears and residual financing gap.

4/ Following a price rule, oil revenue from 2005 onward is projected on the basis of an international price estimated to be US\$2 lower than the latest WEO forecasts. Alternatively, using WEO price forecasts would increase oil revenue and generate windfall oil revenues.

5/ Nonreschedulable debt service only, excluding IMF but including oil-collateralized debt.

Table 9. Republic of Congo: Monetary Survey, 2001–04

	2001	2002				2003				2004			
		Mar.	Jun.	Sep.	Dec.	Mar.	Jun.	Sep.	Dec.	Mar.	Jun.	Sep.	Dec.
		Actual				Actual	Est.			Projections			
(In billions of CFA francs)													
Net foreign assets	26.9	23.8	49.5	54.5	38.0	39.3	53.7	8.3	6.0	6.3	6.7	7.0	7.3
Central bank	23.9	18.2	29.1	44.7	-0.9	27.6	-3.2	-6.5	4.6	4.9	5.3	5.6	5.9
Deposit money banks	3.0	5.6	20.5	9.8	38.9	11.7	56.9	14.8	1.4	1.4	1.4	1.4	1.4
Net domestic assets	231.1	222.3	217.1	236.0	253.7	231.7	218.2	265.5	278.6	287.5	290.1	288.8	295.1
Net domestic credit	267.2	268.3	239.6	229.6	249.7	226.8	219.6	251.9	265.0	274.0	276.5	275.2	281.5
Net credit to the public sector	158.2	167.8	175.8	158.9	183.3	155.0	150.0	175.2	183.3	190.9	192.2	189.6	194.7
Net credit to the government	163.5	172.8	178.0	171.7	186.8	144.5	151.8	180.2	187.8	195.5	196.7	194.2	199.2
Central bank	160.3	162.4	170.3	171.1	173.9	158.7	188.4	186.0	182.1	187.2	186.0	183.4	188.5
Deposit money banks	3.2	10.3	7.7	0.6	12.8	-14.2	-36.6	-5.8	5.8	8.3	10.8	10.8	10.8
Claims on public agencies, net	-5.3	-5.0	-2.2	-12.9	-3.4	10.5	-1.8	-5.0	-4.5	-4.5	-4.5	-4.5	-4.5
Credit to the economy	109.0	100.5	63.8	70.7	66.4	71.8	69.6	76.7	81.7	83.0	84.3	85.6	86.9
Other items, net	-36.1	-46.0	-22.5	6.4	4.0	4.8	-1.4	13.5	13.6	13.6	13.6	13.6	13.6
Broad money	258.0	246.1	266.6	290.5	291.7	271.0	271.9	273.8	284.6	293.9	296.7	295.8	302.5
Currency outside banks	142.9	126.0	137.1	127.0	129.0	103.5	110.7	108.0	131.9	132.4	133.7	133.2	136.2
Demand deposits	95.2	103.8	114.8	140.7	142.2	137.7	115.4	119.8	103.2	112.2	113.3	113.0	115.5
Time deposits	19.9	16.2	14.7	22.8	20.5	29.8	45.8	46.0	49.4	49.2	49.7	49.6	50.7
(Changes in percent of beginning-of-year broad money)													
Net foreign assets	-37.3	-1.2	8.8	10.7	4.3	0.4	5.4	-10.2	-11.0	0.1	0.2	0.4	0.5
Net domestic assets	14.5	-3.4	-5.4	1.9	8.8	-7.5	-12.2	4.0	8.5	3.1	4.0	3.6	5.8
Net domestic credit	3.0	0.4	-10.7	-14.6	-6.8	-7.9	-10.3	0.7	5.2	3.1	4.0	3.6	5.8
Net credit to the government	21.0	3.6	5.6	3.2	9.0	-14.5	-12.0	-2.3	0.4	2.7	3.1	2.2	4.0
Credit to the economy	-16.4	-3.3	-17.5	-14.8	-16.5	1.9	1.1	3.5	5.3	0.5	0.9	1.4	1.8
Broad money	-22.8	-4.6	3.3	12.6	13.1	-7.1	-6.8	-6.1	-2.4	3.3	4.3	3.9	6.3
Memorandum items:													
Velocity													
Total GDP/average M2	6.9	...	...	...	7.7	...	...	...	7.1	...	...	...	7.3
Non-oil GDP/average M2	3.0	...	...	...	3.6	...	...	...	3.6	...	...	...	3.6
Non-oil GDP/end period M2	3.4	...	...	...	3.3	...	...	...	3.6	...	...	...	3.6
Total GDP growth (in percent)	-10.9	...	...	...	2.9	...	...	...	-3.0	...	...	...	5.2
Non-oil GDP growth (in percent)	12.0	...	...	...	10.4	...	...	...	6.1	...	...	...	6.3
Credit to the economy/non-oil GDP	12.3	...	...	...	6.8	...	...	...	7.9	...	...	...	7.9

Sources: BEAC; and Fund staff calculations.

Table 10. Republic of Congo: Balance of Payments, 2000–07
(In billions of CFA francs)

	2000	2001	2002	2003	2004	2005	2006	2007
	Projections							
Current account	182.0	-64.6	-6.9	6.0	-113.2	-136.0	-143.0	-141.8
Trade balance	1,319.7	1,007.1	1,075.1	1,003.8	955.7	851.8	829.8	825.9
Exports, f.o.b.	1,743.8	1,506.6	1,567.3	1,475.6	1,455.2	1,360.9	1,365.1	1,389.8
Oil sector	1,633.2	1,341.4	1,373.8	1,225.7	1,184.5	1,068.8	1,047.8	1,039.4
Non-oil sector	110.6	165.2	193.5	249.9	270.7	292.1	317.3	350.4
Imports, f.o.b.	-424.1	-499.5	-492.2	-471.8	-499.5	-509.0	-535.3	-564.0
Oil sector	-70.3	-179.3	-70.1	-70.1	-56.6	-48.0	-51.4	-54.4
Government	-91.9	-123.2	-108.4	-81.2	-107.4	-115.2	-123.3	-131.5
Non-oil private sector	-262.0	-197.0	-313.7	-320.4	-335.5	-345.9	-360.6	-378.0
Balance of services	-478.5	-462.8	-514.0	-492.8	-436.4	-393.8	-394.6	-398.4
Oil sector	-381.9	-358.8	-352.4	-352.3	-281.0	-236.7	-234.8	-237.4
Non-oil sector	-96.6	-104.1	-161.6	-140.5	-155.4	-157.1	-159.8	-161.0
Income	-672.6	-611.3	-570.7	-508.8	-638.1	-597.7	-582.1	-573.5
Labor income	-16.6	-19.2	-21.7	-13.2	-15.1	-13.7	-14.1	-13.3
Investment income	-656.0	-592.0	-549.0	-495.6	-623.0	-584.0	-567.9	-560.3
<i>Of which: interest on public debt</i>	-149.2	-144.3	-122.8	-89.8	-204.5	-200.5	-206.4	-212.2
Current transfers (net)	13.4	2.3	2.7	3.8	5.6	3.6	3.9	4.2
Private	5.0	-1.9	-1.7	-0.6	0.2	-1.0	-0.8	-0.5
Public	8.4	4.2	4.4	4.3	5.3	4.6	4.7	4.7
<i>Of which: technical assistance</i>	0.1	2.6	2.2	2.0	1.7	2.1	2.0	2.0
Capital account	14.3	69.2	10.7	11.1	19.2	19.4	19.9	20.2
Official grants	6.8	3.7	3.7	9.9	18.0	18.4	18.7	19.1
Debt cancellation	6.5	63.6	6.4	0.1	0.0	0.0	0.0	0.0
Other	1.0	1.9	0.7	1.2	1.2	1.0	1.2	1.1
Financial account	-35.1	-107.2	36.1	-11.7	65.1	55.5	140.2	144.2
Direct investment (net)	340.2	160.0	171.9	187.4	208.6	181.6	156.9	158.3
<i>Of which: oil sector</i>	286.9	152.1	147.8	150.9	177.5	148.3	120.4	121.1
Portfolio investment	0.2	-5.3	-5.9	-3.7	-4.9	-4.8	-4.5	-4.8
Other investment	-375.5	-262.0	-129.9	-195.5	-138.5	-121.3	-12.2	-9.4
Medium and long term	-116.4	-206.5	107.3	-70.1	55.8	42.0	124.8	133.0
Public sector	36.6	-44.1	189.4	11.5	129.4	110.2	193.2	200.0
Drawings	44.0	73.4	234.1	21.6	38.5	39.3	40.1	40.9
Project	8.0	1.3	20.0	13.9	38.5	39.3	40.1	40.9
Program	36.0	28.0	0.0	7.7	0.0	0.0	0.0	0.0
Other (collateralized)	0.0	44.1	214.1	0.0	0.0	0.0	0.0	0.0
Amortization	-292.7	-233.6	-259.7	-174.5	-175.5	-197.4	-123.3	-107.9
Net change in arrears	282.6	104.5	210.8	163.1	266.4	268.3	276.5	267.0
Debt rescheduling	2.8	11.6	4.3	1.4	0.0	0.0	0.0	0.0
Private sector	-153.0	-162.4	-82.1	-81.6	-73.6	-68.2	-68.5	-66.9
Oil	-132.7	-158.4	-77.0	-68.7	-66.4	-59.9	-58.7	-58.2
Non-oil sector	-20.3	-4.0	-5.1	-12.9	-7.2	-8.3	-9.8	-8.7
Short term	-259.2	-55.4	-237.3	-125.4	-194.3	-163.2	-136.9	-142.4
Errors and omissions	-41.1	-1.8	-64.7	0.0	0.0	0.0	0.0	0.0
Overall balance of payments	120.1	-104.4	-24.8	5.5	-28.8	-61.2	17.1	22.6
Financing	-120.1	104.4	24.8	-5.5	-1.3	-16.8	-20.4	-22.1
Reserve financing	-120.1	104.4	24.8	-5.5	-1.3	-16.8	-20.4	-22.1
IMF (net)	9.9	-0.9	-6.0	-5.2	-6.3	-7.6	-2.6	-1.2
Purchases	9.9	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Repurchases	0.0	-0.9	-6.0	-5.2	-6.3	-7.6	-2.6	-1.2
Other reserves	-130.0	105.3	30.8	-0.3	5.0	-9.2	-17.8	-20.9
Financing gap	0.0	0.0	0.0	0.0	30.2	78.0	3.3	-0.5

Sources: BEAC; and Fund staff estimates and projections.

Table 11. Republic of Congo: External Debt Outstanding and Scheduled Debt Service, 2000-07

	2000	2001	2002	2003	2004	2005	2006	2007
	(In billions of CFA francs)							
Total medium- and long-term debt outstanding	3,741.9	4,010.3	3,767.3	3,766.9	3,889.9	3,992.6	4,183.2	4,382.0
<i>Of which:</i> arrears	1,793.5	2,282.6	2,242.5	2,405.6	2,671.9	2,940.3	3,216.8	3,483.8
Excluding IMF	3,712.8	3,981.5	3,744.4	3,749.1	3,878.5	3,988.7	4,181.9	4,381.9
Multilateral	421.4	376.6	382.3	366.3	347.0	333.0	320.0	307.7
Paris Club creditors	2,104.8	2,231.1	2,116.8	2,173.2	2,212.2	2,245.9	2,277.7	2,302.9
Other official creditors	206.2	152.6	141.8	142.5	181.0	220.3	260.4	297.4
Commercial banks	547.5	852.0	726.6	726.6	726.6	726.6	726.6	726.6
Collateralized loans	319.9	247.5	258.2	220.7	170.9	88.1	75.2	64.2
Other private creditors	113.0	121.6	118.7	119.6	120.4	120.8	121.1	121.4
Interest on arrears	...	...	...	...	120.3	253.9	400.9	561.7
IMF credit outstanding	29.1	28.8	22.9	17.8	11.5	3.9	1.3	0.1
Debt service due (including IMF)	442.3	379.6	389.1	269.6	386.7	405.8	332.5	321.3
Principal	292.7	234.5	265.7	179.7	181.8	205.0	126.0	109.1
<i>Of which:</i> IMF	0.0	0.9	6.0	5.2	6.3	7.6	2.6	1.2
Interest	149.6	145.1	123.3	89.9	204.9	200.8	206.6	212.2
<i>Of which:</i> arrears	0.0	0.0	0.0	0.0	120.3	133.6	147.0	160.8
IMF	0.3	0.3	0.3	0.3	0.4	0.2	0.2	0.0
Multilateral	49.3	42.7	44.5	35.7	34.0	28.4	21.8	18.8
<i>Of which:</i> IMF	0.3	1.7	6.5	5.3	6.7	7.8	2.8	1.2
Bilateral	235.0	192.2	177.5	168.4	165.1	149.2	139.8	115.6
Paris Club pre-cutoff date	194.4	161.0	151.1	137.8	137.1	126.3	121.2	100.5
Paris Club post-cutoff date	28.4	25.4	22.1	25.8	23.8	18.5	14.3	13.2
Non-Paris Club	12.2	5.9	4.2	4.8	4.1	4.4	4.3	1.9
Commercial banks	7.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Collateralized loans	134.9	129.3	151.4	54.4	62.5	89.3	17.6	14.8
Other private (including supplier's credits)	10.4	15.5	15.7	11.1	4.8	4.1	4.0	3.9
Arrears and new borrowing (including financing gap)	0.0	0.0	0.0	0.0	120.3	134.8	149.4	168.3
Debt rescheduling	2.8	11.6	4.3	1.4	0.0	0.0	0.0	0.0
Debt service	1.2	3.3	4.3	1.4	0.0	0.0	0.0	0.0
Principal	0.4	2.0	1.8	1.4	0.0	0.0	0.0	0.0
Interest	0.8	1.4	2.4	0.0	0.0	0.0	0.0	0.0
Arrears	1.6	8.3	0.0	0.0	0.0	0.0	0.0	0.0
Debt cancellation	6.5	63.6	6.4	0.1	0.0	0.0	0.0	0.0
Debt service	6.5	4.7	6.4	0.1	0.0	0.0	0.0	0.0
Principal	6.4	4.7	1.7	0.1	0.0	0.0	0.0	0.0
Interest	0.1	0.0	4.6	0.0	0.0	0.0	0.0	0.0
Arrears	0.0	59	0.0	0.0	0.0	0.0	0.0	0.0
Memorandum items:					(In percent)			
External public debt/GDP (including IMF)	163.2	196.3	179.1	184.7	181.3	189.9	192.6	192.8
External public debt/exports (including IMF)	203.3	245.1	222.1	234.3	243.8	264.9	275.0	281.1
Debt service/exports (before debt relief)	24.0	23.2	22.9	16.8	24.2	26.9	21.9	20.6
Principal	15.9	14.3	15.7	11.2	11.4	13.6	8.3	7.0
Interest	8.1	8.9	7.3	5.6	12.8	13.3	13.6	13.6

Sources: Caisse Congolaise d'Amortissement; and Fund staff estimates and projections.

Table 12. Republic of Congo: Elements of the Capacity to Pay External Debt, 2003-07
(In billions of CFA francs, unless otherwise indicated)

	2003 Est.	2004 Proj.	2005 Proj.	2006 Proj.	2007 Proj.
Domestic revenue	603.6	585.6	577.1	593.1	617.7
Oil	421.6	385.6	358.4	352.0	353.4
Non-oil	182.0	200.0	218.7	241.1	264.3
Domestic primary expenditure 1/	-464.5	-460.4	-484.6	-504.0	-523.9
Current	-352.7	-340.3	-354.6	-364.0	-373.9
Capital	-111.8	-120.1	-130.0	-140.0	-150.0
Basic primary fiscal balance	139.1	125.2	92.4	89.1	93.8
Core debt service	-111.1	-128.5	-151.2	-72.0	-67.9
Domestic	-23.4	-14.8	-22.8	-21.2	-22.2
External 2/	-87.7	-113.7	-128.4	-50.9	-45.6
Fiscal balance after core debt service	28.0	-3.3	-58.8	17.1	25.9
Identified financing	36.5	11.4	-3.0	-3.0	-3.0
Domestic 3/	28.8	11.4	-3.0	-3.0	-3.0
External	7.7	...	...	...	...
Fiscal balance after identified financing	64.5	8.1	-61.8	14.1	22.9
Identified arrears payments	-64.6	-38.3	-15.0	-15.0	-15.0
Domestic 4/	-57.6	-38.3	-15.0	-15.0	-15.0
External	-7.0	...	...	...	...
Residual fiscal balance	0.0	-30.2	-76.8	-0.9	7.9
Memorandum items:					
External payment arrears	2405.6	...	...	...	...
Multilateral creditors	102.7	...	...	...	...
Paris Club (post-cutoff date)	268.0	...	...	...	...
Paris Club (pre-cutoff date)	1039.0	...	...	...	...
Other bilateral creditors	125.2	...	...	...	...
Commercial banks and other private creditors	870.7	...	...	...	...
Stock of domestic arrears	557.9	...	...	...	...
Reschedulable debt stock (excluding arrears)	798.1	...	...	...	...
Oil collateralized debt stock	220.7	170.9	88.1	75.2	64.2
Debt service due on reschedulable debt	153.7	146.1	134.8	129.5	106.2
Oil price (in U.S. dollars per barrel)					
World Economic Outlook	29.0	28.7	27.0	26.0	25.5
Price rule	29.0	28.7	25.0	24.0	23.5
Congolese crude	27.4	27.1	23.4	22.4	21.9
Oil production (in millions of barrels)	81.7	84.3	86.7	89.1	91.6
Potential windfall oil revenue	...	...	27.4	28.1	28.9
Basic primary fiscal balance (in percent of GDP)	30.1	28.1	28.3	28.2	28.0
Basic non-oil primary fiscal balance (in percent of non-oil GDP)	11.4	10.1	10.8	10.8	10.6

Sources: Congolese authorities; and Fund staff estimates and projections.

1/ Excluding interest payments and foreign-financed investment.

2/ Debt service due on post-cutoff date to Paris Club creditors, to multilateral creditors, and on oil-collateralized debt; excluding potential impact of Paris Club rescheduling.

3/ Includes exceptional oil revenue from settlement with private oil companies.

4/ Related to wages, pensions, and small- and medium-sized enterprises.

Table 13. Republic of Congo: External Financing Requirements, 2000–07
(In billions of CFA francs, unless otherwise indicated)

	2000	2001	2002	2003 Est.	2004	2005	2006	2007
	Projections							
Requirements	290.2	199.8	311.0	178.3	295.4	354.9	291.4	276.6
Current account excluding official transfers	-173.6	68.8	11.3	-1.7	118.5	140.6	147.7	146.6
Debt amortization	292.7	233.6	259.7	174.5	175.5	197.4	123.3	107.9
IMF repurchases	0.0	0.9	6.0	5.2	6.3	7.6	2.6	1.2
Change in net foreign assets (increase +) 1/	130.0	-105.3	-30.8	0.3	-5.0	9.2	17.8	20.9
Adjustment 2/	41.1	1.8	64.7	0.0	0.0	0.0	0.0	0.0
Resources	290.2	199.8	311.0	178.3	295.4	354.9	291.4	276.6
Official transfers	8.4	4.2	4.4	4.3	5.3	4.6	4.7	4.7
Official project grants	7.8	5.6	4.4	11.1	19.2	19.4	19.9	20.2
Long-term public loan disbursements	44.0	73.4	234.1	21.6	38.5	39.3	40.1	40.9
Program	36.0	28.0	0.0	7.7	0.0	0.0	0.0	0.0
Project	8.0	1.3	20.0	13.9	38.5	39.3	40.1	40.9
Other 3/	0.0	44.1	214.1	0.0	0.0	0.0	0.0	0.0
Private capital (net)	-71.7	-63.1	-153.3	-23.2	-64.2	-54.7	-53.0	-55.8
Debt relief	9.3	75.2	10.6	1.5	0.0	0.0	0.0	0.0
Use of IMF resources	9.9	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Change in arrears (increase +)	282.6	104.5	210.8	163.1	266.4	268.3	276.5	267.0
Residual financing gap	0.0	0.0	0.0	0.0	30.2	78.0	3.3	-0.5
Memorandum item:								
Exchange rate (CFA francs per U.S. dollar, average)	712.0	733.0	697.0	580.1	...	...	...	...

Sources: Congolese authorities; and Fund staff estimates and projections.

1/ Excluding the change in the net position vis-à-vis the Fund.

2/ Errors and omissions.

3/ Collateralized borrowing.

Table 14. Republic of Congo: Millennium Development Goals, 1990–2015

	1990	1995	2001	2002	2015 Target
Goal 1. Eradicate extreme poverty and hunger					
Target 1: Halve, between 1990 and 2015, the proportion of people whose income is less than one dollar a day.					
1. Population below US\$1 a day (percent)	...	...	...	...	...
2. Poverty gap ratio at US\$1 a day (percent)	...	...	...	...	...
3. Share of income or consumption held by poorest 20 percent (percent)	...	...	...	...	...
Target 2: Halve, between 1990 and 2015, the proportion of people suffering from hunger.					
4. Prevalence of child malnutrition (percent of children under 5)	...	...	...	...	...
5. Population below minimum level of dietary energy consumption (percent)	37.0	...	32.0	...	[18.5]
Goal 2. Achieve universal primary education					
Target 3: Ensure that, by 2015, children will be able to complete a full course of primary schooling.					
6. Net primary enrollment ratio (percent of relevant age group)	...	...	...	...	...
7. Percent of cohort reaching grade 5	62.3	55.1	...	...	...
8. Youth literacy rate (percent ages 15-24)	92.5	95.6	97.6	97.8	[100.0]
Goal 3. Promote gender equality and empower women					
Target 4: Eliminate gender disparity in primary and secondary education preferably by 2005 and to all levels of education by 2015.					
9. Ratio of girls to boys in primary and secondary education (percent)	87.5	96.7	89.1	...	...
10. Ratio of young literate females to males (percent ages 15-24)	95.2	97.6	98.7	98.8	...
11. Share of women employed in the nonagricultural sector (percent)	...	...	...	...	...
12. Proportion of seats held by women in the national parliament (percent)	14.0	2.0	12.0	12.0	...
Goal 4. Reduce child mortality					
Target 5: Reduce by two-thirds, between 1990 and 2015, the under-five mortality rate.					
13. Under-five mortality rate (per 1,000)	110.0	108.0	108.0	...	[73.3]
14. Infant mortality rate (per 1,000 live births)	83.0	81.0	81.0	75.0	...
15. Immunization against measles (percent of children under 12-months)	75.0	38.0	35.0	...	...
Goal 5. Improve maternal health					
Target 6: Reduce by three-quarters, between 1990 and 2015, the maternal mortality ratio.					
16. Maternal mortality ratio (modeled estimate, per 100,000 live births)	...	1,100.0	...	...	...
17. Proportion of births attended by skilled health personnel	...	...	...	...	...
Goal 6. Combat HIV/AIDS, malaria and other diseases					
Target 7: Halt by 2015, and begin to reverse, the spread of HIV/AIDS.					
18. HIV prevalence among females (percent ages 15-24)	...	...	7.8	...	...
19. Contraceptive prevalence rate (percent of women ages 15-49)	...	...	...	...	...
20. Number of children orphaned by HIV/AIDS	...	...	78,000.0	...	...
Target 8: Halt by 2015, and begin to reverse, the incidence of malaria and other major diseases.					
21. Prevalence of death associated with malaria	...	...	...	...	...
22. Share of population in malaria risk areas using effective prevention and treatment	...	...	...	...	...
23. Incidence of tuberculosis (per 100,000 people)	...	...	338.2	...	...
24. Tuberculosis cases detected under DOTS (percent)	...	79.0	97.0	...	...

Table 14. Republic of Congo: Millennium Development Goals, 1990–2015 (concluded)

	1990	1995	2001	2002	2015 Target
<u>Goal 7. Ensure environmental sustainability</u>					
Target 9: Integrate the principles of sustainable development into policies and programs. Reverse the loss of environmental resources.					
25. Forest area (percent of total land area)	65.1	...	64.6	...	
26. Nationality protected areas (percent of total land area)	...	4.5	4.5	5.0	
27. GDP per unit of energy use (PPP \$ per kg oil equivalent)	1.7	2.7	3.3	...	
28. CO2 emissions (metric tons per capita)	0.9	0.7	0.8	...	
29. Proportion of population using solid fuels					
Target 10: Halve by 2015 proportion of people without access to safe drinking water.					
30. Access to improved water source (percent of population)	...	...	51.0	...	
Target 11: Achieve by 2020 significant improvement for at least 100 million slum dwellers.					
31. Access to improved sanitation (percent of population)	...	...	14.0	...	
32. Access to secure tenure (percent of population)	...	...	...	...
<u>Goal 8. Develop a Global Partnership for Development 1/</u>					
Target 16: Develop and implement strategies for productive work for youth.					
45. Unemployment rate of population ages 15-24 (total).	...	...	...	...
Target 17: Provide access to affordable essential drugs.					
46. Proportion of population with access to affordable essential drugs	...	...	...	...
Target 18: Make available new technologies, especially information and communications.					
47. Fixed line and mobile telephones (per 1,000 people)	...	8.6	55.3	...	
48. Personal computers (per 1,000 people)	...	...	3.9	...	

Sources: World Bank; and Fund staff estimates.

1/ Targets 12-15 and indicators 22-44 are excluded because they cannot be measured on a country-specific basis. These are related to official development assistance, market access, and the HIPC Initiative.

Republic of Congo: Relations with the Fund
 (As of March 31, 2004)

I. Membership Status: Joined: 07/10/1963; Article VIII

II. General Resources Account:

	<u>SDR Million</u>	<u>%Quota</u>
Quota	84.60	100.00
Fund holdings of currency	93.33	110.32
Reserve tranche position	0.54	0.63

III. SDR Department:

	<u>SDR Million</u>	<u>%Allocation</u>
Net cumulative allocation	9.72	100.0
Holdings	0.10	1.07

IV. Outstanding Purchases and Loans:

	<u>SDR Million</u>	<u>%Quota</u>
ESAF arrangements	6.95	8.21
Credit tranche	9.25	10.94

V. Latest Financial Arrangements:

<u>Type</u>	<u>Approval Date</u>	<u>Expiration Date</u>	<u>Amount Approved (SDR Million)</u>	<u>Amount Drawn (SDR Million)</u>
PRGF	06/28/1996	06/27/1999	69.48	13.90
Stand-by arrangement	05/27/1994	05/26/1995	23.16	12.50
Stand-by arrangement	08/27/1990	05/26/1992	27.98	4.00

VI. Projected Obligations to Fund: (SDR million; based on existing use of resources and present holdings of SDRs):

	<u>2004</u>	<u>2005</u>	<u>Forthcoming</u>		
			<u>2006</u>	<u>2007</u>	<u>2008</u>
Principal	5.36	8.07	2.78		
Charges/interest	0.28	0.25	0.16	0.15	0.15
Total	5.64	8.32	2.94	0.15	0.15

VII. Implementation of HIPC Initiative:

The Republic of Congo is likely to be eligible to debt relief under the HIPC Initiative, once it establishes a track record under a PRGF-supported program. The timing of a possible PRGF arrangement will depend on performance under the staff-monitored program covering the period January–June, 2004.

VIII. Safeguards Assessments:

An on-site safeguards assessment of the Bank of the Central African States (BEAC), of which Republic of Congo is a member, was completed on July 20, 2001 (see Appendix V). The assessment concluded that high risks may exist in the financial reporting framework and internal audit mechanism and made recommendations as reported in the safeguards assessments report. In a letter dated July 11, 2001, the BEAC authorities committed to implementing most of the recommendations, progress on which is monitored by staff.

IX. Exchange Rate Arrangement:

Congo's currency is the CFA franc, which is pegged to the euro at a fixed rate of CFAF 655.957 = euro 1. On April 1, 2004, the rate of the CFA franc was CFAF 791.73 per SDR. Congo does not impose any restrictions on the making of payments and transfers for current international transactions.

X. Article IV Consultations:

Consultations with Congo are on the standard 12-month cycle. The 2003 consultation discussions were held in Brazzaville in February/March 2003. The staff report (Country report No. 03/193) was considered by the Executive Board on June 13, 2003.

XI. FSAP Participation :

N/A.

XII. Technical Assistance :

Subject	Department	Staff Member	Date
Modernization of tax and customs administrations	FAD	Gilles Montagnant-Rentier, Eric Lesprit and Ahmed Boilil	February 2004
Follow-up mission	FAD	Mr. Lepage	November 2003

Subject	Department	Staff Member	Date
Budget functional classification	FAD	Messrs. Bouley, Hélise, and Lepage	October 2003
Multisector statistics	STA	Messrs. Marie, Maiga, and Mmes. Fisher, Matei, Razin, and Balvani	May 2002
Resident expert on statistics	STA	Mr. Sin	Since October 2001
Balance of payments	STA	Mr. Fiévet	June 2001
Budget, tax, and customs	FAD	Messrs. Bouley, Moussa, Brik, and Mrs. Tricoire	April–May 2001
Resident tax expert	FAD	Mr. Laurent	1995–97
Tax administration	FAD	Mr. Grandcolas	November 1995–April 1996
Tax administration	FAD	Mr. Grandcolas and Mr. Castro	November 1994
Budget, expenditure classification			Request under consideration

XIII. Resident Representative:

A senior resident representative took up his assignment in September 1995, but was recalled to headquarters shortly after the outbreak of the civil strife in June 1997.

Republic of Congo: Relations with the World Bank Group
(As of December 31, 2003)

The World Bank reengaged in Congo in early 2001 within the context of a Transitional Support Strategy (TSS) aimed at (i) supporting the Government in facing the challenges of consolidating civil peace; (ii) laying and solidifying the foundation for the democratization of political life; (iii) rehabilitating social and economic infrastructure; and (iv) improving economic management, including increased transparency and good governance in the oil sector.

A. The Bank Group Strategy and Lending Operations

On August 8, 2001, the Republic of Congo cleared all its overdue service payments to IBRD and IDA. All IBRD loans and IDA credits to the Republic of Congo have been restored to accrual status and the country's eligibility for disbursements under existing loans, credits, project preparation facility advances and for new operations, was reinstated. Bank assistance to Congo resumed and the field mission reopened. As a result, and in line with the TSS, the Bank has been supporting Congo with a variety of operations including (i) a Post-conflict Economic Rehabilitation Credit (PERC) for SDR 30 million¹⁰ (in July 2001) to support implementation of key structural reforms, help to better manage fiscal resources, and assist in improving governance and transparency in the oil sector; (ii) an Emergency Demobilization and Reintegration Credit for SDR 4 million (also in July 2001) to facilitate the reintegration of about 10,000 ex-combatants into civil life; (iii) an Infrastructure Rehabilitation and Improvement in Living Conditions Credit for SDR 32.2 million (in April 2002) to rehabilitate key infrastructure (including portions of the key railroad link, roads and health facilities) and help mitigate unemployment through a variety of labor-intensive micro-projects; and (iv) a Governance and Transparency Capacity Building Credit for SDR 5.6 million (in February 2002) to accompany reforms supported by the Post Conflict Economic Rehabilitation Credit.

An Emergency Reconstruction and Community Support Credit to assist communities living in smaller municipalities and rural areas has been approved by the Board in June 2003. An Economic Recovery Credit to sustain and deepen economic reforms initiated under PERC, as well as an HIV/AIDS project to be financed by grants, are scheduled to be presented to the Board by the end of FY 2004. An education project is also under preparation.

Under non-lending services, the Bank is preparing a Public Expenditure Management Review to help improve fiscal management, and is assisting the Congo in preparing its interim poverty reduction strategy paper. An Institutional Development Grant has been approved to support the rehabilitation of statistical capacity.

¹⁰ Fully disbursed.

The updated Transitional Support Strategy (TSS) for FY2004-5 has been presented to the Board and approved in September 2003. Its main objective is to help the Congo get out of the conflict trap. The current TSS has four strategic elements:

- Promote economic growth and diversification through: (i) supporting economic reforms, particularly in the context of access to PRGF; (ii) rebuilding infrastructure; (iii) enhancing education and professional training; and (iv) supporting rural development.
- Help strengthen and reposition the public sector through advisory services and adjustment operations, with a focus on: (i) increasing transparency in the oil sector; improving public resource management; and (iii) enhancing capacity.
- Help mitigate short-and medium-term social and political risks by: (i) supporting demobilization and reintegration of former combatants; and (ii) assisting in the fight against HIV/AIDS.
- Assist in increasing resources for peace and development by helping the Congo in benefiting from the HPIC initiative, and obtaining support from other donors.

B. IMF-World Bank Collaboration in Specific Areas

The IMF and World Bank staff maintain a close collaborative relationship in supporting policies to consolidate civil peace and recover from a decade of recurring conflicts, sustain macro-economic stability, improve governance, reverse a marked decline in social indicators, and promote sustainable development. Exchange of information and discussion on progress in the implementation of the reform program take place on a regular basis between the Bank and the Fund. Joint missions are carried out to review progress.

Areas where the World Bank leads and there is no direct IMF involvement:

- health and education sectors, for which two projects are under preparation;
- state disengagement from productive sectors through privatization/restructuring of public utilities enterprises and commercial banks; and
- more transparent use of public funds through the reform of public procurement and the institution of a special body (*Cour des Comptes*).

Areas where the World Bank leads and its analysis serves as input to the IMF:

- review of selected issues in the oil sector, including the recently completed audit of the oil company (SNPC) and the follow up action plan;
- forestry management;
- social policies;
- assistance in PRSP preparation;

- governance and taxation in the forestry sector; and
- public expenditure review.

Areas of shared responsibility:

- governance in the oil sector;
- efficient use of public resources;
- oil revenue mobilization;
- public finance management;
- governance and fiscal impact of large investment projects;
- preparatory work on HIPC issues; and
- statistics and measurement issues.

Areas where the IMF takes the lead and its analysis serves as an input to the World Bank:

- competitiveness/exchange rate issues;
- tax policy and administration; and
- custom tariffs/protectionism.

Areas where the IMF takes the lead and there is no direct World Bank involvement:

- fiscal policy;
- monetary and credit issues;
- external payments regime;
- non-oil revenue mobilization; and
- macroeconomic statistics issues.

Brazzaville, March 31, 2004

Ms. Anne O. Krueger
Acting Managing Director
International Monetary Fund
Washington, D.C. 20431
U.S.A.

Dear Ms. Krueger:

1. On behalf of the government of the Republic of Congo, I am pleased to send you herewith the memorandum on economic and financial policies. This memorandum describes recent economic developments, the implementation of the 2003 staff-monitored program (SMP), and the measures that the government undertakes to implement in 2004 with a view to strengthening macroeconomic management.
2. The government recognizes that, despite encouraging results, the overall implementation of the 2003 SMP was weak, especially in the fiscal area and governance in the oil sector. The government remains, nevertheless, convinced that an improvement of the country's economic and financial position is indispensable to attain the strong and lasting growth necessary for poverty reduction, and that the implementation of a program supported by resources from the Poverty Reduction and Growth Facility (PRGF) is the best way to achieve those objectives. As a result, the government has decided to adopt another SMP, which it intends to implement rigorously during the first half of 2004 in order to strengthen the framework that would permit an agreement to be reached on an arrangement that can be supported by the PRGF.
3. The two principal objectives of this new program are to strengthen fiscal discipline and enhance transparency in fiscal management, particularly in the oil sector. The gradual improvement in administrative capacity and the commitment of the government to avoid the slippages of the past constitute assurances that this program will succeed. The government requests the support of Fund staff for the monitoring of the proposed program.
4. The government is aware that the satisfactory implementation of the new SMP will be necessary but not sufficient for embarking on a PRGF arrangement. Indeed, in addition to its own efforts, the government is also counting on the support of its development partners for assistance in addressing the budgetary financing gap, which is largely attributable to the external debt burden. In this context, the government believes that an exceptional treatment of the country's external debt payment arrears by the international community will be necessary, including on arrears to multilateral institutions and Paris Club creditors on post-cutoff-date debt.

5. An interim poverty reduction strategy is being drafted on the basis of broad civil society participation. The government plans to adopt this strategy in a timely manner and to submit it to its development partners to seek their support for its implementation, including debt relief under the Heavily Indebted Poor Countries (HIPC) Initiative.

6. The government will provide the Fund with any information it may request for monitoring the implementation of economic and financial policies and the achievement of the program objectives, as described in the technical memorandum of understanding attached to the memorandum on economic and financial policies. The government is committed to disseminating this memorandum and authorizes the Fund to publish it on its website.

Sincerely yours,

/s/

Rigobert R. Andély
Minister of Economy, Finance, and Budget

Attachments: Memorandum on Economic and Financial Policies for 2004
Technical Memorandum of Understanding

REPUBLIC OF CONGO

Memorandum on Economic and Financial Policies

Brazzaville, March 31, 2004

I. INTRODUCTION

1. The Republic of Congo, a post-conflict country, is determined to strengthen its economic and financial medium-term framework in order to achieve sustained growth and initiate lasting poverty reduction. The government recognizes that performance in the implementation of previous Fund-supported programs has generally been below expectations. The reasons for this disappointing performance include (i) the inherited sluggishness of the planned economy, which has long had a negative impact on the private sector; (ii) the civil wars of the 1990s which disrupted the economy, weakened the institutions, and undermined the rule of law; (iii) the weakness of economic management during the transition period that followed the war; and (iv) insufficient ownership of program implementation by the government.
2. With the completion of the democratization process in 2002 and the signing of the peace agreements with the rebel groups in 1999 and 2003, the government began implementing its Nouvelle Espérance (New Hope) economic and social program based on consolidating economic management and poverty reduction, strengthening institutional capacity, and improving transparency and governance.
3. In 2003, the government adopted and implemented a staff-monitored program (SMP) that was geared to lead to a program supported under the International Monetary Fund's (IMF's) Poverty Reduction and Growth Facility (PRGF). Despite encouraging results, there have generally been major weaknesses in the implementation of this program, especially as regards fiscal discipline and transparency in oil sector management. Conscious of the need to build a sound economic basis for achieving sustainable poverty reduction, the government has decided to adopt a new SMP covering the first half of 2004. This memorandum on economic and financial policies describes the objectives of that program and the actions envisaged for achieving them.
4. After five years of domestic efforts to reconstruct the country destroyed by war, the Congolese government is seeking the support of the international community in the form of technical assistance, further financing, and rescheduling of the country's external debt on exceptional terms, including the arrears that are nonreschedulable.

II. IMPROVED SECURITY

5. The Congo is emerging from some ten years of political instability, marked by three civil wars that have led to enormous human loss, the exodus of a portion of the population, and the destruction of entire villages, buildings, infrastructure, and units of production. These

wars have exacerbated the preexisting shortcomings in public management, particularly in fiscal and oil revenue management. In the social sectors, many facilities and much equipment were destroyed or looted. The socioeconomic fabric has been seriously torn, and the proportion of the population living below the poverty line rose sharply.

6. Recent developments on the political and security fronts have involved considerable improvements. The political transition period, which began at the end of the war in 1997, was completed in August 2002 after the presidential, legislative, and communal elections. Out of an interest in consolidating peace, the government and representatives of the remainder of the rebellion signed a peace agreement on March 17, 2003, pursuant to which demilitarization, demobilization, and reintegration operations started, with support from the international community. The speed with which the country is being rebuilt and democratic institutions are being installed, using only domestic resources, raises much hope, and the government is making efforts to restore sound macroeconomic management and promote transparency.

7. The overall debt situation has worsened because a portion of the spending on reconstruction and elections was financed through oil-backed borrowing. In addition, during the period 1999–2001, the oil revenue reported by the treasury fell short by about CAF 174 billion of the oil companies' fiscal liabilities to the government, as stipulated in the production-sharing contracts. This was related to the use of extrabudgetary resources to finance reconstruction and humanitarian projects, as well as sovereignty-related outlays, such as elections, security, and national reconciliation.

III. RECENT ECONOMIC DEVELOPMENTS

8. The return of peace has stimulated economic activity in the non-oil sector, particularly in agriculture, forestry, trade, and transportation. Non-oil real GDP grew by about 6 percent in 2003. The consumer price inflation rate decelerated to 1.6 percent in 2003 from 3.1 percent in 2002 as a result of the strengthening of the euro and the regular supply of consumer goods, attributable to the resumption of rail traffic between Pointe-Noire and Brazzaville. In the oil sector, high world prices have offset the decline in production, thereby increasing government oil revenue. These additional resources have helped finance an appreciable expansion of the public investment program. In 2003, for the first time in three years, credit to the private sector grew faster than non-oil GDP, partly as a result of a catch-up to more normal activities.

9. The fiscal position improved in 2003 compared with 2002, but by less than the approved budget suggested. The basic primary fiscal surplus increased from 1.2 percent of GDP in 2002 to 6.8 percent in 2003 (the 2003 budget had targeted a surplus of 9.3 percent). The improvement in the fiscal balance in 2003 is essentially attributable to the reduction of total expenditure and higher-than-expected oil revenue. The main budget execution weaknesses included, *inter alia*, weak tax revenue collection, larger-than-expected transfers, and unbudgeted payments for domestic arrears related to both the social sector and reconstruction investment. However, for the first time in two decades, the government did not resort to collateralized borrowing against future oil revenue, and, as a result of payments

made in 2003, the stock of such debt is now smaller. In light of the exceptionally high debt service related to those loans in 2003, the government was, however, obliged to defer to 2004 a number of payments due.

10. The external current account was in broad balance in 2003; indeed, oil exports, expressed in CFA francs, fell only slightly compared with 2002, as the decline in oil production was offset by the rise in oil prices, while public sector imports and external debt service decreased. Faced by the deterioration in the Congo's rate of external reserves coverage (and even though for all Central African Economic and Monetary Community—CEMAC—countries combined the rate was 64 percent), the regional head office of the Bank of Central African States (BEAC) in Yaoundé tightened its control of private sector current transfers and gradually reduced, to zero in June 2003, the threshold above which its prior authorization is required. Nevertheless, the BEAC head office decided to relax this policy as of January 2004, and the rate of acceptance of transfer requests has increased.

11. The large volume of external debt arrears remains an obstacle to the full normalization of relations between the Republic of Congo and its creditors. Indeed, on December 31, 2003, the stock of public external debt totaled approximately US\$7 billion (185 percent of GDP), about 65 percent of which represented arrears. However, efforts were made in 2003 to (i) ensure the regular and timely payment of the current maturities of service on the debt that is not eligible for rescheduling (except for one Paris Club creditor who received only a portion of the service due on its post-cutoff-date debt), and (ii) begin paying off the stock of external arrears to multilateral creditors.

IV. IMPLEMENTATION OF THE STAFF-MONITORED PROGRAM IN 2003

12. The Congolese government recognizes that, overall, performance under the SMP covering the period January-September 2003 was unsatisfactory. The program was implemented vigorously in the first quarter of 2003, but performance deteriorated steadily in the following two quarters.

13. Fiscal performance was generally weak (Table 1); indeed, the basic primary fiscal surplus, adjusted to take account of favorable trends in oil prices compared with program estimates, fell short of the program objective by about CFAF 57 billion between January and September 2003 (2.8 percent of annual GDP). This shortfall was primarily a result of five factors: (i) the shortfall in nonoil revenue; (ii) transfers to the national oil refinery (CORAf) not foreseen under the program; (iii) failure by the national oil company (SNPC) to transfer to the state treasury on a timely basis oil revenue due to the government; (iv) higher-than-programmed subsidization of petroleum products; and (v) prices realized by the SNPC on the sale of the fiscal oil it received on behalf of the government that were below the reference price. In addition, the exceptional oil revenue derived from the settlement of a dispute between the Congolese government and private oil companies (representing 1.3 percent of GDP) and unprogrammed oil bonus and dividend yields (equivalent to 0.4 percent of GDP) were used for the unplanned clearance of large amounts of domestic arrears related to the social sector and public reconstruction projects.

14. On the structural side, performance was mixed (Tables 2 and 3). Noteworthy progress was achieved with the completion in July 2003 of the audit of the SNPC's 1999–2001 accounts. Considerable efforts were made to centralize public revenue and expenditure in the budget; to stop incurring debt collateralized by future oil revenue; and, for the first time in two decades, to publish in the interest of transparency, oil sector data and improve the macroeconomic statistics. In addition, the external payment arrears owed to a few multilateral institutions were cleared. On the other hand, the Congo paid only about 80 percent of the current service due on the 2003 debt not eligible for rescheduling; the privatization of Crédit pour Agriculture, l'Industrie, et le Commerce (CAIC) was not completed; and certain other measures planned for end-September 2003 to increase oil sector transparency (the publication of production-sharing contracts, the SNPC's 2003 budget, and the audit report on the SNPC's 2001 accounts) were not implemented.

V. DEVELOPMENTS IN THE FOURTH QUARTER OF 2003

15. The government took measures to stabilize the fiscal position, and progress was made in the implementation of structural measures in the last quarter of 2003 (Tables 4 and 5). The basic primary fiscal balance target was slightly exceeded as a result of higher oil revenue and the savings on transfers and investment expenditure. However, unprogrammed expenses were made in the fourth quarter, in particular for the payment of pension arrears and to cover the costs of structural reforms (CFAF 8 billion). The certification by an external auditor of government oil revenue for the period January-September 2003 is an important step toward oil sector transparency. Other structural reforms in the fiscal area have been implemented, including the following: (i) the appointment of new directors in the General Directorates of Budget, Customs, and Taxes, as well as at the General Inspectorate of Finance, to reinvigorate the revenue departments and strengthen control; (ii) the signing of the government/SNPC/CORAF agreement, which drastically reduced the subsidies to be paid to CORAF; and (iii) the production of the 2000 budget review law (*Loi de règlement*).

VI. POVERTY REDUCTION FRAMEWORK AND MEDIUM-TERM STRATEGY

16. The government is determined to place poverty reduction at the center of its strategy. The primary objectives of this policy can be found in the interim poverty reduction strategy paper (I-PRSP) being drafted by the government. To achieve these objectives, the government is targeting an average real growth rate of about 3½-4 percent during the period 2004–06. The expected upturn in oil production and sound performance by the non-oil sectors, in particular agriculture, forestry, and the processing industries, will contribute to this growth. The rate of inflation is projected at 2 percent on average over the period, assuming sound fiscal policy, the pursuit of a prudent monetary policy by the BEAC, and a smooth traffic flow between Pointe-Noire and Brazzaville. Following the expected increase in oil and non-oil exports, the current account balance should improve over the medium term.

17. The government will in the future avoid procyclical fiscal expenditure related to oil revenue. It expects to achieve this objective, starting in 2005, by adopting a rule for forecasting oil revenue that is based on prudent price assumptions and by gradually

establishing a medium-term public expenditure framework consistent with the objectives of the I-PRSP. Clear rules for the allocation of budgetary resources will be established, and special attention will be paid to the fiscal deficit, with a view to reducing government borrowing gradually. In addition, nonpriority current expenditure will be better controlled through (i) the revival of the mechanism of quarterly ceilings for each ministry, strengthened as of 2004 by a new budgetary commitment procedure based on the weekly availability of resources, and (ii) the ongoing enhancement of the tracking of "service performed."

18. In the next few years, the public investment program financed with domestic resources will be dominated by a few major projects with the following priority objectives: (i) to ensure a regular supply of electricity in the country (the building of Imboulou Dam and restoration of the Mokoukoulou Dam); (ii) to strengthen the public infrastructure and open up the interior of the country (road networks and Ollombo Airport); (iii) to improve basic social services; and (iv) to enhance infrastructure in local communities (safe water, schools, and dispensaries).

19. In order to ensure the financing of its development and poverty reduction program, the government plans to maximize the mobilization of domestic resources. In this regard, the ratio of non-oil revenue to non-oil GDP is expected to rise from 17.6 percent in 2003 to 19.5 percent by 2007. In addition, the government plans to undertake the regular and efficient monitoring of oil receipts due by oil companies to the state treasury. The government will ensure that all the revenue generated by the settlement of the disputes with the oil companies is transferred to the treasury and shown in the budget. In 2003, exceptional oil revenue from the settlement of the disputes with one oil company totaled US\$215 million, US\$145 million of which was paid during the year in cash and in increased oil rights.

VII. OBJECTIVES FOR 2004

20. The principal quantitative targets for 2004 are as follows: (i) real economic growth of 3.6 percent, (ii) an annual average inflation rate of 2 percent, (iii) a basic primary fiscal balance representing 5.8 percent of GDP, and (iv) a current account deficit equal to 1.5 percent of GDP.

21. The government program agreed with the Fund was prepared on the basis of revenue estimates totaling CFAF 585.6 billion (27.3 percent of GDP). The petroleum sector revenue estimate is based on the assumption of a volume of oil production totaling 84.3 million barrels, a world price of US\$28.7 dollars a barrel, and an exchange rate of CFAF 515.5 = US\$1. The government is committed to using additional oil receipts resulting from higher-than-programmed prices to finance the budgetary gap, as well as to accelerating external arrears payments in its efforts to normalize relations with creditors. Non-oil revenue is estimated to reach CFAF 200 billion (18.2 percent of nonoil GDP). In the event that the oil price or the non-oil revenue is lower than envisaged, the government will take the necessary actions to lower expenditures via a revised budget law.

22. Efforts are under way to make poverty reduction and the strict control of unproductive expenditures the main aim of public expenditure policy. The expected rise in the wage bill (approximately CFAF 4 billion more in 2004 than in 2003) is a result of social sector recruitment plans and the reintegration into the civil service payroll of employees of the former General Directorate of Credit and Financial Relations. Total traditional transfer payments are expected to increase considerably relative to 2003, principally owing to the establishment of institutions in support of democratization, including the Audit Office, the High Court of Justice, the National Commission on Human Rights, and the Economic and Social Council.

23. Domestic payment arrears are to be settled in an equitable and transparent manner. All domestic payment arrears of a commercial nature as of end-2002 have been audited. The government plans to complement this work with an audit of social debt and the adoption and publication of a policy and settlement plan for all domestic arrears. The implementation of this plan will follow budgetary procedures and will depend on the availability of financial resources. To improve the social environment for productive activity, the government signed with the unions a "social truce," whereby gradual payment of wage and retirement pension arrears will begin in 2004. To this end, the 2004 budget law provides for the payment of CFAF 23.3 billion to wage earners and retirees and a package of CFAF 15 billion for the settlement of other domestic priority arrears.

24. For 2004, a residual financing gap is projected (excluding treatment of the stock of external arrears and current service due on reschedulable external debt), totaling CFAF 30.2 billion. The government expects that this gap will be financed through (i) budgetary support from development partners; and (ii) the release of residual resources from the legal settlement of disputes with a private oil company. In the event that these resources are not all forthcoming or prove insufficient to bridge the gap, the government has drawn up a contingency list of expenditure items, the execution of which will be deferred.

VIII. STAFF-MONITORED PROGRAM

25. The new SMP covers the period January-June 2004. The two principal pillars of the new program relate to the strengthening of fiscal discipline and transparency in fiscal management, particularly in the oil sector (Tables 6 and 7; see paras. 23-29 of the technical memorandum of understanding for the technical details of the structural measures).

A. Fiscal Policy

26. Fiscal policy is being implemented in line with the spirit of the 2004 budget law, that is, it will seek to increase non-oil revenue and ensure strict expenditure management.

27. As regards oil revenue, the government is committed to ensuring that all revenue payable to the state is immediately transferred to the treasury. Oil revenue estimates and the sums actually received by the treasury will be systematically cross-checked. To this end, the size of the staff of the Oil Revenue-Monitoring Unit in the Ministry of Finance is to be increased.

28. Measures are being taken to achieve a sustained increase in non-oil revenue. In this regard, the implementation of a customs warehouse and exemption control program has already started. In addition, by end-July 2004, the principal measures envisaged are as follows: (i) establishment of the single taxpayer identification number; (ii) introduction of new computerized customs clearance procedures (SYDONIA); and (iii) establishment of a computer link between the revenue departments in Pointe Noire and Brazzaville.

29. Expenditures are to be executed in conformity with normal budgetary procedures. Accordingly, advance payments and the awarding of contracts by mutual agreement (*gr     *) will be reduced to a strict minimum. Over time, it is planned that all contracts above CFAF 10 million will be awarded through a competitive bidding process. In addition, the Treasury is being strengthened through the assignment by the French Cooperation of public accounting experts; the January 2004 provisional balance will be available at end-March 2004. Finally, the government will gradually introduce a functional classification system for expenditure that will permit the earmarking of a greater portion of public spending for poverty reduction programs. Preliminary versions of this system for classifying operating and capital expenditure will be available by June 2004.

B. Oil Sector Reform

30. The government is convinced that transparency and accountability in oil sector operations are essential to the improvement of governance and sound fiscal management. Components of the reforms in this sector are as follows:

- **Maximizing revenue collection.** First, the government undertakes to continue the quarterly certification, by an internationally recognized audit firm with the collaboration of the Oil Revenue-Monitoring Unit in the Ministry of Finance, of oil revenues, a process started in 2003. Second, a clear policy on dividend payments to the public treasury by the SNPC will be adopted by the government by end-March 2004. The policy will ensure that the SNPC limits its costs and focuses on its core activities in order to produce the maximum return on public resources invested in the oil sector. Third, the government plans to regularly order independent audits of the costs of oil companies, so as to ensure that the latter pay all their financial liabilities to the Treasury.
- **Monitoring the SNPC's operations.** The external audit of the SNPC's 1999-2001 accounts and operations for the government pointed to shortcomings, including in accounting practices, internal controls, and the provision of information to the government on the marketing of government oil and financial transactions carried out for the government. To remedy these shortcomings, a comprehensive action plan is being drawn up, in consultation with World Bank and IMF staff. Progress made in the implementation of this plan will be checked through the conclusions of the recommendations made in the annual external audit reports. A strategy for restoring the focus of the SNPC on its basic activity will be drafted and adopted by the government by end-June 2004.

- **Improving transparency.** The government will continue to increase the amount of information made available to the public through internet sites, including the publication of the revenue certification reports, information on oil sector operations, and the external audit reports.

31. The government undertakes to carry out the reform of the CORAF, subsidies to which continue to be a drain on the government budget. The financial statements of the CORAF at end-2002 will be audited in 2004. The results of this audit will help in the preparation of a reform strategy for the company. Meanwhile, a ceiling of CFAF 8 billion has been set on budgetary subsidies to this company in the 2004 budget.

32. Finally, the subsidization of petroleum products will henceforth be established objectively and managed efficiently. A key objective is to gradually eliminate the subsidies, while being mindful of the impact on the poorest segments of the population. To this end, the government will seek the assistance of the World Bank to assess the cost and efficiency of the current system of setting prices at the pump, including the subsidy granted, and will propose alternative mechanisms. The study will analyze, among other things, the modalities of establishing a mechanism for automatic price adjustments, depending on world prices. Where applicable, it will propose a system of subsidies for the most underprivileged segments of the population, which are expected to be the most affected by these adjustments.

C. Other Structural Reforms

33. In the banking sector, the process of privatizing CAIC will be completed by end-June 2004; the participation of the strategic international investor, already approved by the regional banking supervisory commission (COBAC), is expected to be formalized with the payment of its capital share. In addition, with technical assistance from the World Bank, the government will begin discussions on the formulation of a reform policy for the insurance sector, which is facing serious financial problems. The government recognizes the importance of the reforms aimed at ensuring the continued growth in the microcredit sector and the recent expansion of credit to the private sector. To this end, the government will maintain the tax exemption for microfinance mutual associations, a subsector that has been flourishing in the postwar period.

34. Implementation of the program to restructure/privatize public enterprises will continue with World Bank assistance. The actions envisaged for the short term relate to an acceleration of the reforms in the water, electricity, telecommunications, and rail transport sectors. The aim is to improve the quality and lower the cost of these services, so as to make them more accessible, to promote economic activity, and to improve living conditions for the people. With respect to rail transport, the bids received for the award of the Chemin de Fer Congo-Océan (CFCO) concession are being assessed, and the government intends to divest the operation of this company to the private sector by end-2004.

IX. TECHNICAL ASSISTANCE

35. The capacity-building needs of the Republic of Congo are vast, given the destruction caused by several years of war. As a result, the implementation of the planned economic program cannot succeed without substantial assistance from development partners. The government welcomes the technical assistance already provided by the international community, including the IMF in the fiscal and statistics areas. However, given the enormous task at hand in the area of fiscal reform, the government needs long-term resident experts, including in the areas of tax and customs administration and expenditure programming and management. The other areas in which the needs are pressing include the following: (i) the formulation of a strategy to settle domestic and external arrears; (ii) support for the Program Technical Monitoring Committee, and the Oil Revenue-Monitoring Unit at the Ministry of Finance; and (iii) the strengthening of control procedures and structures and for inspection in the revenue departments.

X. PROGRAM MONITORING

36. The implementation of the program will be monitored on a quarterly basis by means of the quantitative and structural indicators described in Tables 6 and 7 and the attached technical memorandum of understanding.

Table 1. Republic of Congo: Quantitative Indicators, 2002-03
(In billions of CFA francs, unless otherwise indicated; cumulative from January)

	2002				2003				Sep.			
	Dec.		Mar.		Jun.		Prog.		Init.		Rev.	
	Act.	Prog.	Rev.	Prog.	Act.	Prog.	Rev.	Act.	Proj.	Proj.	Adj.	Proj.
Net claims of the banking system on the central government (ceiling) 1/	163	159	159	127	159	160	133	159	161	161	161	162
New medium- and long-term nonconcessional external debt (including leasing) contracted or guaranteed by the government (ceiling) 2/ 3/	217	0	0	0	0	0	0	0	0	0	0	0
New nonconcessional debt (including leasing) with an original maturity of less than one year (ceiling) 3/ 4/	0	0	0	0	0	0	0	0	0	0	0	0
Stock of external arrears 5/	2,394	2,423	2,423	2,422	2,469	2,469	2,469	2,496	2,504	2,504	2,504	2,501
Net reduction in domestic arrears (floor; - =increase)	10	0	0	8	0	0	0	35	0	40	40	38
Primary fiscal balance (floor) 6/	26	34	62	78	81	112	116	136	131	173	173	116
Central government wage bill (ceiling)	120	30	30	30	60	60	61	90	91	91	91	91
Memorandum items:												
Oil revenue	398	94	122	143	188	219	278	281	327	369	327	
Debt relief	11	0	...	0	0	...	1	0	1	...	...	...
Nonproject external financing	217	0	...	0	0	...	0	0	0	0	...	...
External debt arrears change (cumulative)	212	28	...	28	75	...	0	101	110	...	...	106
Payment of external arrears	6	0	...	6	0	...	6	0	0	0	0	6
Petroleum price (Brent; U.S. dollars per barrel), cumulative average	25	22	...	31	22	...	29	22	22	22	22	29
Exchange rate (CFA francs per U.S. dollar)	697	670	...	611	670	...	594	670	670	670	670	591
Petroleum price (Brent; thousands of CFA francs per barrel), cumulative average	17.4	14.7	...	19.2	14.7	...	17.2	14.7	14.7	14.7	14.7	17.0

1/ Excluding IMF credit. The indicator will be adjusted downward for the higher-than-projected relief on scheduled debt-service payments.

2/ Excluding rescheduling arrangements and disbursements from the Fund, but including debt with maturities of more than one year.

3/ Concessional debt is defined as debt with a grant element of at least 50 percent, calculated on the basis of currency-specific discount rates, based on the OECD commercial interest reference rates (CIRRs).

4/ On a contracting or guaranteed basis. Excluding debt related to normal import transactions.

5/ The target will be adjusted downward to reflect higher-than-expected nonproject financing and debt relief, and upward for lower-than-expected nonproject financing and debt relief.

6/ Defined as revenue excluding grants, minus noninterest current expenditures, domestically financed capital expenditure, and net lending, on a commitment basis. It will be adjusted upward for higher-than-expected oil revenue, calculated as a ratio of projected oil revenue times actual oil price divided by projected oil price (in CFA francs).

Table 2. Republic of Congo: Structural Indicators, January–June 2003

Measures	Schedule	Status
Payment of all debt service due to multilateral creditors and of debt service due on nonreschedulable debt to Paris Club creditors.	Continuously	Not done. All payments effected on time, with the exception of arrears to the AFD (Agence Française de Développement).
Submission by the external auditors to the government of the draft report (as stipulated in contract) on the national oil company's (SNPC)'s 1999–2000 accounts and its 2001 consolidated accounts.	June 2003	Done.
Submission by the SNPC to the government of its 2002 consolidated financial statements, as required by law.	June 2003	Not done.
Completion of the privatization of the CAIC (commercial bank).	June 2003	Not done.
Report on an in-depth evaluation of the effectiveness of the June 2001 convention between the government and the SNPC (following the outline provided by IMF staff).	May 2003	Done.
Audit of the off-budget capital expenditures during 2000–02.	June 2003	Done.
Centralization of all government revenues in, and execution of all payments through, the treasury account.	Continuously	Not done. The national oil refinery (CORAFO) did not pay for the government's oil while the SNPC withheld part of oil revenue due to the treasury.
No settlement of budget expenditures through the direct transfer of government revenue by oil companies.	Continuously	Done.
No contracting of any form of oil-collateralized debt (new or refinanced).	Continuously	Done.
Monthly provision to the IMF staff of all information necessary for the monitoring of the program.	Continuously	Done.

Table 3. Republic of Congo: Structural Indicators, July–September 2003

Measures	Schedule	Status
Cease payments of domestic arrears, with the exception of those relating to social debt (pensions, salaries, and small and medium-sized enterprises). 1/	Continuously	Done.
Put under the supervision of the Ministry of Finance a monitoring committee charged with reconciling data prepared by the preshipment inspection company (BIVAC) and customs declarations.	July 15, 2003	Done.
Communicate to oil companies a list of the official treasury bank accounts to which the transfer of oil revenue, including bonuses, should be made.	July 15, 2003	Done.
Adopt an action plan with measures for the national oil company (SNPC) to bring its accounting practices up to international standards, including through the measures recommended by the financial audit undertaken by KPMG, with the objective of preparing financial accounts that would be approved without reservations by auditors.	August 31, 2003	Done.
Create a working group to examine and apply the recommendations of the IMF statistics multisector mission of May 2002.	August 31, 2003	Done.
Create a working group from relevant government departments and agencies (DGDDI, CNSEE, DGCRF, DGE, BEAC, and DG du Commerce) to harmonize external trade statistics.	August 31, 2003	Done.
Prepare a plan for monthly publication of data and information on petroleum-related activities.	August 31, 2003	Done.
Publish on an Internet site the SNPC's 1999 and 2000 balance sheets with annexes listing the company's holdings.	August 31, 2003	Done.
Prepare, for publication, a complete list of 2002 financial transactions carried out by the SNPC on behalf of the government.	August 31, 2003	Done.
Prepare a preliminary report on reconciliation, on a monthly basis, of payments owed to the government by oil companies and payments actually received by the treasury for the period January-June 2003.	August 31, 2003	Done.
Publish on an Internet site the SNPC's 2003 budget.	September 30, 2003	Not done.

Table 3. Republic of Congo: Structural Indicators, July–September 2003

Measures	Schedule	Status
Publish on an Internet site the complete texts of the production-sharing agreements between oil companies and the government.	September 30, 2003	Not done.
Publish on an Internet site the SNPC's 2003 budget.	September 30, 2003	Not done.
Publish on an Internet site the SNPC's 2001 consolidated accounts, as well as the external audits (the opinion of the Auditor General, and the profit and loss statements) and an annex listing the company's holdings.	September 30, 2003	Not done.
Cease all investments by the SNPC unless explicitly approved by the SNPC's executive board.	Continuously	Done.
Pay all debt service due to multilateral creditors and debt service due on nonreschedulable debt to Paris Club creditors.	Continuously	Not done. All payments effected on time, with the exception of arrears to the AFD (Agence Francaise de Développement).
Centralize all government revenues in, and execution of all payments through, the treasury account.	Continuously	Not done. The national oil refinery (CORAF) did not pay for part of the government's oil while the SNPC withheld part of oil revenue due to the treasury. 2/
Do not settle budget expenditures through the direct transfer of government revenue by oil companies.	Continuously	Done.
Do not contract any form of oil-collateralized debt (new or refinanced).	Continuously	Done.
Provide monthly to the IMF staff all information necessary for the monitoring of the program.	Continuously	Done.

1/ The ceilings are as follows: pensions and salaries (CFAF 6 billion), and small and medium-sized enterprises (CFAF 2 billion).

2/ The authorities made a commitment to put in place a convention to regulate the financial relation between CORAF and its oil suppliers, including the government. They are also determined to make effective the rules on supplying oil to CORAF by all involved oil companies.

Table 4. Republic of Congo: Quantitative Indicators, 2002-03
(In billions of CFA francs; cumulative from January)

	Dec. 2002 Actual	December 2003		
		Init. Proj.	Rev. Proj.1/	Est.
Net claims of the banking system on the central government (ceiling) 2/	163	157	162	169
New medium- and long-term nonconcessional external debt (including leasing) contracted or guaranteed by the government (ceiling) 3/ 4/	217	0	0	0
New nonconcessional debt (including leasing) with an original maturity of less than one year (ceiling) 4/ 5/	0	0	0	0
Stock of external arrears 6/	2,394	2,542	2,539	2,559
Net reduction in domestic arrears (floor; -- =increase)	10	0	43	39
Primary fiscal balance (floor)7/	26	191	132	139
Central government wage bill (ceiling)	120	120	121	120
Pour mémoire:				
Oil revenue	398	375	419	422
Debt relief	11	0	1	1
Nonproject external financing	217	0	8	8
External debt arrears change (cumulative)	212	147	145	164
payemenof external arrears	6	0	6	6
Petroleum price (Brent, US\$/barrel), cumulative average	25	22	28	29
Exchange rate (CFAF/US\$)	697	670	588	553
Petroleum price (Brent, thousand CFAF/barrel), cumulative average	17.4	14.7	16.7	16.3

1/ As revised in October 2003.

2/ Excluding IMF credit. The indicator will be adjusted downward for the higher-than-projected relief on scheduled debt service payments.

3/ Excluding rescheduling arrangements and disbursements from the Fund, but including debt with maturities of more than one year.

4/ Concessional debt is defined as debt with a grant element of at least 50 percent calculated on the basis of currency-specific discount rates, based on the OECD commercial interest reference rates (CIRRs).

5/ On a contracting or guaranteed basis. Excluding debt related to normal import transactions.

6/ The target will be adjusted downward to reflect higher-than-expected nonproject financing and debt relief, and upward for lower- than-expected nonproject financing and debt relief.

7/ Defined as revenue excluding grants, minus noninterest current expenditures, domestically financed capital expenditure, and net lending, on a commitment basis. It will be adjusted upward for higher-than-expected oil revenue, calculated as a ratio of projected oil revenue times actual oil price divided by projected oil price (in CFA francs).

Table 5. Republic of Congo: Structural Indicators, October–December 2003

Measures	Schedule	Status
Oil sector		
• Signing of the government/national oil company (SNPC)/national oil refinery (CORAF) agreement for the delivery of crude to CORAF.	December 2003	Done.
• Certification by an external auditor of oil revenue for the period January–September 2003; based on the work of the oil revenue-monitoring unit, the external auditor will ascertain that all oil revenue legally due by oil companies (including the SNPC) was received by treasury.	December 2003	Done.
• Adoption by SNPC's board of directors of a resolution establishing new procedures for the payment of dividends to the government by the SNPC.	December 2003	Not done.
• Completion of internal study on the fuel sector.	December 2003	Done.
Government finance		
• Reorganization of agencies and departments DGI, CCA, and DGB, and treasury internal control.	December 2003	Done.
• Transfer of DGI, DGD, CCA, and DGB personnel.	December 2003	Done.
• Introduction of a functional budget classification module based on the IMF bridge table.	December 2003	Not done. 1/
• Reinforcement of treasury secondary centers.	December 2003	Done
• Production of a provisional treasury balance.	December 2003	Done.

1/ Coding, data entry, and regrouping already completed for the operating budget; work on the investment budget in progress.

Table 6. Republic of Congo: Quantitative Indicators, 2004
(In billions of CFA francs; cumulative from January)

	End-March Prog.	End-June Prog.	End-Sep. Proj.	End-Dec. Proj.
Main quantitative indicators				
Primary fiscal balance (floor) 1/ 2/	12.3	54.4	86.0	125.2
Ceiling on the change in the banking system net credit to the central government (ceiling) 2/ 3/	7.7	8.9	6.4	11.4
New medium- and long-term nonconcessional external debt (including leasing) contracted or guaranteed by the government (ceiling) 4/ 5/ 6/	0.0	0.0	0.0	0.0
New external debt (including leasing) with an original maturity of less than one year (ceiling) 5/ 6/	0.0	0.0	0.0	0.0
New oil-based collateralized debt (ceiling) 6/	0.0	0.0	0.0	0.0
External arrears payment (floor) 2/	0.0	0.0	0.0	0.0
New external arrears on nonreschedulable debt 6/	0.0	0.0	0.0	0.0
Domestic arrears payment (ceiling) 6/ 7/	6.0	10.8	17.8	38.3
New domestic arrears 6/ 7/	0.0	0.0	0.0	0.0
Other quantitative indicators				
Nonoil revenue	38.2	82.9	136.1	200.0
Central government wage bill (ceiling)	30.5	61.8	93.1	124.5
Domestically-financed investment	34.7	59.5	95.3	120.1
Memorandum items				
Oil revenue (billions of CFA francs)	87.4	184.6	288.7	385.6
Nonproject external financing 2/	...	...	...	...
Petroleum price (Brent, US\$/barrel), quarterly average	30.0	28.7	28.4	27.6
Exchange rate (CFA francs/US\$), quarterly average	516.5	515.1	512.5	517.9
Petroleum price Brent (thousand CFAF/barrel, quarterly average)	15.5	14.8	14.6	14.3
Oil production (million barrels, quarterly average)	20.4	19.7	21.5	22.7
Of which: Government's share traded by SNPc	6.7	4.6	5.1	4.3

1/ See paragraph 5 of the Technical Memorandum of Understanding (TMU) for the definition.

2/ See paragraphs 20 and 21 of the TMU on the adjustors.

3/ Including IMF credit.

4/ Excluding rescheduling arrangements and disbursements from the IMF.

5/ See paragraph 11.b of the TMU for the definition of concessional debt.

6/ Continuous performance criterion.

7/ See paragraphs 17 and 18 of the TMU for the definition.

Table 7. Republic of Congo: Structural Indicators for the Staff-Monitored Program

Measures	Schedule
Certification by an external auditor of oil revenue for the fourth quarter of 2003; based on the work of the oil-monitoring unit, the external auditor will ascertain that all oil revenue legally due by oil companies (including the SNPC) was received by treasury. 1/	March 31, 2004
Publication by the government on an Internet site of the external auditor's full report on oil revenue reconciliation for the first half of 2003.	March 31, 2004
Adoption by the government of an action plan for the implementation of all the recommendations of the audit of the SNPC, prepared with the assistance of the World Bank and IMF.	March 31, 2004
Adoption by the government of a fully articulated and operational policy on the payment of dividends by the SNPC, prepared with the assistance of the World Bank and IMF; policy to be published on an Internet site.	March 31, 2004
Publication by the government, on an Internet site, of the August 1, 2003 summary of the report on the 1999–2001 audit of the SNPC prepared by the auditing firm, as well as (i) the 108 recommendations of the audit report, (ii) the action plan for the implementation of the recommendations from the SNPC audit (see above); (iii) Chapter 4 of the audit report, and (iv) the comments of the SNPC.	March 31, 2004
Preparation by the government of the consolidated fiscal treasury balance for January 2004.	March 31, 2004
Publication by the government, on an Internet site, of the production sharing agreements (PSAs) already published in the Official Gazette, a list of the PSAs that were not published, and an explanation of how these PSAs relate to the various production fields.	April 15, 2004
Publication by the government on an Internet site of a complete list of the financial transactions carried out by the SNPC on behalf of the government in 2002 and 2003 (including the dates of transactions, amounts, interest rates and commissions, and terms and conditions).	April 30, 2004
Preparation by the government of a preliminary strategy aimed at ensuring that the SNPC's activities are restricted to the oil sector.	June 30, 2004
Completion, by an international external auditing firm, of the 2002 external audit of the SNPC (according to the same terms of reference as the previous audit and with no qualifications related to access to information). 2/	July 31, 2004

Table 7. Republic of Congo: Structural Indicators for the Staff-Monitored Program

Measures	Schedule
Signing by the government of a contract with an international auditing firm to perform the external financial audit of the 2002 operations of the national oil refinery (CORAF).	August 31, 2004
Signing by the government of a three-year contract with an international firm to perform the annual external audits of the SNPC for 2003–05 (using the same terms of reference as for the previous audit). 2/	August 31, 2004
Quarterly certification, by an external auditor, of oil revenue in 2004, using the same terms of reference as for the 2003 certifications. Reports to be published on an Internet site on a timely basis.	With a one-quarter lag
Centralization of all government revenues in, and execution of all payments through, the treasury.	Continuous
No settlement of public expenditures through the direct transfer of government revenue by oil companies.	Continuous

1/ Using the same terms of reference as for the certifications in previous quarters of 2003.

2/ Financial audits of consolidated financial statements, review of financial flows, review of execution of the management contract, and review of internal control. Publication of the 2002 external audit report will follow the same modalities as the 1999–2001 report.

Table 8. Republic of Congo: Government Budgetary Operations, 2003-04
(In billions of CFA francs; cumulative from January)

	2003	2004			
		Est.	End-March Prog.	End-June Prog.	End-Sep. Proj.
Domestic revenue	603.6	125.6	267.5	424.8	585.6
Oil	421.6	87.4	184.6	288.7	385.6
Non-oil	182.0	38.2	82.9	136.1	200.0
Primary expenditure	464.5	113.3	213.1	338.8	460.4
Current 1/	352.7	78.6	153.6	243.5	340.3
Capital 2/	111.8	34.7	59.5	95.3	120.1
Primary budget balance	139.1	12.3	54.4	86.0	125.2
Debt service due 3/	-111.1	-39.2	-83.2	-105.2	-128.5
Domestic	-23.4	-3.7	-7.4	-11.1	-14.8
External non-reschedulable debt service	-87.7	-35.5	-75.8	-94.1	-113.7
Multilaterals	-30.5	-9.3	-13.1	-23.1	-27.4
Paris Club, post cut-off date	-10.0	-0.5	-11.7	-12.1	-23.8
Collateralized debt	-47.2	-25.7	-51.0	-59.0	-62.5
Balance after debt service	28.0	-26.9	-28.8	-19.2	-3.3
Identified financing	36.5	38.4	39.6	26.4	11.4
Domestic (net)	28.8	7.7	8.9	6.4	11.4
Banking system	1.0	7.7	8.9	6.4	11.4
Nonbank financing	27.8	0.0	0.0	0.0	0.0
Of which: Exceptional oil receipts 4/	59.2	...	...	...	...
Statistical float 5/	-3.3	0.0	0.0	0.0	0.0
External	7.7	30.7	30.7	20.0	0.0
Non-projet loans	7.7	...	...	...	...
Advance payment on oil shipment	...	30.7	30.7	20.0	0.0
Residual balance before arrears payment (+ = surplus)	64.5	11.5	10.8	7.2	8.1
Arrears payments	-64.6	-6.0	-10.8	-17.8	-38.3
Domestic	-57.6	-6.0	-10.8	-17.8	-38.3
External	-7.0	...	...	...	...
Residual balance	0.0	5.5	0.0	-10.7	-30.2

Sources: Congolese authorities; and staff estimates and projections.

1/ Excluding interest

2/ Excluding foreign-financed investment.

3/ Nonreschedulable debt only.

4/ Revenue stemming from the settlement of a legal dispute with a private oil company.

5/ Including errors and omissions.

REPUBLIC OF CONGO

Technical Memorandum of Understanding

Brazzaville, March 31, 2004

1. This memorandum establishes the modalities for monitoring the staff-monitored program agreed between the International Monetary Fund (IMF) and the government of the Republic of Congo for the period from January 1 to June 30, 2004.

I. QUANTITATIVE INDICATORS

2. The primary quantitative indicators are the following:
 - a. a minimum basic primary fiscal balance, starting January 1, 2004;
 - b. a ceiling on the change in the banking system's net credit to the government (excluding net IMF credit), starting January 1, 2004;
 - c. no new medium- or long-term nonconcessional external debt (including leasing) contracted or guaranteed by the government, starting January 1, 2004 (indicator to be monitored continuously);
 - d. no new external debt (including leasing) with a maturity of less than one year contracted or guaranteed by the government, starting January 1, 2004 (indicator to be monitored continuously);
 - e. no new debt collateralized by crude oil deliveries, starting January 1, 2004 (indicator to be monitored continuously);
 - f. payment of a minimum amount of external arrears (floor), starting January 1, 2004;
 - g. no accumulation (in gross value) of new external payment arrears, excluding external debt service due that is eligible for rescheduling, starting January 1, 2004 (indicator to be monitored continuously);
 - h. a ceiling on payments of domestic debt arrears, starting January 1, 2004; and
 - i. no accumulation (in gross value) of new domestic arrears, starting January 1, 2004.
3. The other quantitative indicators are as follows:
 - a. a minimum threshold for non-oil and nontax revenues, starting January 1, 2004;
 - b. a ceiling on the government wage bill, starting January 1, 2004; and

- c. a ceiling on public investments financed with domestic resources, starting January 1, 2004.

II. DEFINITIONS AND COMPUTATION

A. Government, and Basic Primary Fiscal Balance

4. Unless otherwise indicated, “government” is defined as the central government of the Republic of Congo. The scope of the government’s fiscal operations table (TOFE) includes the general budget, the special accounts of the treasury and the government debt management agency (Caisse Congolaise d’Amortissement, CCA).
5. The government’s basic primary fiscal balance is equal to total revenue excluding grants, minus total expenditure excluding interest payments and capital expenditure financed with external resources. It is measured on the basis of the budget execution reported every month in the TOFE prepared by the Ministry of Finance. At end-2003, the basic primary fiscal balance was estimated at CFAF 139.1 billion, resulting from total revenue (excluding grants) of CFAF 603.7 billion and total expenditures (excluding interest on the debt and capital expenditure financed with external resources) of CFAF 464.6 billion.
6. The government’s total revenue is valued on a cash basis. It includes all revenue (tax revenue, oil revenue, and nontax revenue collected by the treasury). Total revenue also takes into account the gross revenue of the special accounts. Oil revenue excludes all forms of prepayment and prefunding (see definitions below).
7. Expenditure is valued on a payment order basis. It includes current expenditure, domestically financed capital expenditure, externally financed capital expenditure, and net lending. Current expenditure is defined as the difference between total expenditure and capital expenditure and net lending. Current expenditure is broken down into personnel expenditure, expenditure on goods and services, interest on the debt (domestic and external), transfers and subsidies, and other current expenditure.

B. Change in Net Position of the Government

8. The government’s net position vis-à-vis the banking system (including net IMF credit) is defined as the balance between the central government’s claims on, and debts to, domestic banking institutions. The claims of the central government include the cash balances of the treasury, deposits at the Bank of Central African States (BEAC), deposits at commercial banks, and central government deposits at the Caisse Nationale d’Epargne (CNE) and the Centre des Chèques postaux (CCP). Treasury liabilities with the banking system include BEAC lending (including statutory advances and consolidated advances), lending from commercial banks (including government securities held by the commercial banks), and CNE/CCP deposits.

9. The end-of-period stock of net bank claims on the government, excluding the counterpart of the use of Fund resources, is valued in accordance with the accounting

framework currently used by the BEAC. At December 31, 2003, these claims amounted to CFAF 169 billion.

C. Debt and External Arrears

10. The definition of government used for the external debt performance criterion includes government, as defined in paragraph 4, and government agencies.

11. For the purposes of this memorandum, the definitions of "debt" and "concessional borrowing" are as follows:

- a. As specified in point 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt adopted by the Executive Board of the IMF on August 24, 2000, debt will be understood to mean a current, that is, not contingent, liability, created under a contractual arrangement through the provision of value in the form of assets (including currency) or services, and which requires the obligor to make one or more payments in the form of assets (including currency) or services, at some future point(s) in time; these payments will discharge the principal and/or interest liabilities incurred under the contract. Debts can take a number of forms, the primary ones being as follows: (i) loans, that is, advances of money to the obligor by the lender made on the basis of an undertaking that the obligor will repay the funds in the future (including deposits, bonds, debentures, commercial loans, and buyers' credits) and temporary exchanges of assets that are equivalent to fully collateralized loans under which the obligor is required to repay the funds, and usually pay interest, by repurchasing the collateral from the buyer in the future (such as repurchase agreements and official swap arrangements); (ii) suppliers' credits, that is, contracts where the supplier permits the obligor to defer payments; and (iii) leases, that is, arrangements under which property is provided that the lessee has the right to use for one or more specified periods of time that are generally shorter than the total expected service life of the property, while the lessor retains the title to the property. For the purpose of the guideline, the debt is the present value (at the inception of the lease) of all lease payments expected to be made during the period of the agreement, excluding those payments that cover the operation, repair, or maintenance of the property. Under the definition of debt set out above, arrears, penalties, and judicially awarded damages arising from the failure to make payment under a contractual obligation that constitutes debt are debt. Failure to make payment on an obligation that is not considered debt under this definition (e.g., payment on delivery) will not give rise to debt.
- b. Loan concessionality is assessed on the basis of the commercial interest reference rates (CIRRs) established by the OECD. A loan is said to be on concessional terms if, on the initial date of disbursement, the ratio of the present value of the loan, calculated on the basis of the reference interest rates, to its nominal value is less than 50 percent (i.e., a grant element of at least 50 percent). For debts with a maturity exceeding 15 years, the ten-year reference interest rate published by the OECD is

used to calculate the grant element. For shorter maturities, the six-month market reference rate is used.

12. The indicator with respect to external debt applies not only to debt as defined in point 9 of the Guidelines on Performance Criteria with Respect to Foreign Debt but also to commitments contracted or guaranteed for which no value has yet been received or on which only partial drawings have been made. However, this indicator does not apply to financing from the IMF or to treasury bills and bonds issued in CFA francs on the CEMAC regional market.¹¹

13. For external debt with a contractual maturity of less than one year, loans associated with imports and exports are excluded from the scope of the indicator.

14. The accumulation of external payment arrears is the difference between (i) the gross amount of external debt service payments due (principal and interest, including penalty interest, as appropriate) and (ii) the amount actually paid during the period under consideration. Payment arrears to creditors for which the government is actively seeking debt relief in good faith are excluded from the external payment arrears for purposes of program monitoring. The stock of external debt payment arrears is assessed at the end of the period, and the amounts in foreign currency are converted to CFA francs based on the exchange rates published by the IMF. Under the program, the government undertakes not to accumulate external payment arrears on its debt, with the exception of external payment arrears arising from government debt being renegotiated with external creditors, including bilateral creditors who are not members of the Paris Club. The accumulation of new arrears is the amount due but unpaid on the due dates during the period of the program. Nonaccumulation of external payments arrears is an indicator to be continuously monitored.

D. Oil-Backed External Debt

15. Prefinancing is defined as a loan backed by oil, that is, advances of money to the debtor by the lender made on the basis of an undertaking that the debtor will surrender to the creditor at a future date the equivalent in oil of the loan plus interest and other fees; the loan is repaid by the sale of the oil in a different fiscal year. New prefintancing (excluding refinancing operations of the existing stock¹² and/or deferral of the service due) is strictly prohibited under the program. The refinancing operation and/or deferrals should not give rise to the augmentation of the existing stock of oil-backed debt.

¹¹ Treasury bills and bonds issued in CFA francs on the CEMAC (Central Africa Economic and Monetary Community) regional market are excluded from the external debt.

¹² The stock of oil-collateralized debt amounted to CFAF 236 billion at end-December 2003, and the government plans to pay down CFAF 54.4 billion in 2004 on this category of debt.

16. A prepayment is an advance of money (from the oil trader) to the government on oil cargoes intended purely for commercial purposes, with a maximum repayment period of six months. This type of financing is designed to enhance cash flow by offsetting any misalignments in receipts and disbursements of funds. Prepayment-related operations must be unwound in the calendar year to which they apply. They are recorded in the accounts as follows:

- At the time the prepayment is obtained, the amounts received are recorded as positive financing (drawings); the amounts corresponding to commissions are recorded as current expenditure.
- The advance is repaid by the sale of the oil; at the time of the repayment transaction, the revenue derived from the sale of the oil is recorded as final oil revenue accruing to the treasury and the amount of the repayment is posted as negative financing (repayment).

E. Arrears and Domestic Debt

17. Cumulative ceilings on domestic payment arrears are fixed. These arrears cover back pay, overdue payments to pension funds, and the audited domestic commercial debt. This latter category of debt is based on the complete list of arrears due at end-2003, which was provided to the IMF. The authorities intend to begin implementing the “social truce” negotiated with the labor unions; when it ends, the outstanding debt on wages and pensions will be settled. Budget appropriations to cover arrears are estimated at CFAF 23.3 billion in 2004—CFAF 14.5 billion for wages in arrears and CFAF 8.8 billion to pay the arrears owed to pension funds (treasury correspondents). Furthermore, a CFAF 15 billion envelope was budgeted for a partial payoff of the audited domestic commercial debt.

18. Net changes in the domestic payment arrears of the central government are equivalent to the difference over the period between the amount of payments authorized and the actual payments made (within 45 days). A net reduction in arrears is reflected in the TOFE as a negative amount and a net accumulation as a positive sum. Payments made by the government cover payments by the treasury, including through clearing operations.

F. Wage Bill

19. The wage bill is defined as the total of all government personnel expenditure, including the wages and statutory benefits of all civil service and military personnel, be they permanent or temporary. The annual wage bill in 2003 is estimated at CFAF 120.2 billion at December 31, 2003.

III. ADJUSTMENTS

20. The basic primary fiscal balance (2a) will be adjusted upward if oil revenue is higher than projected. Oil revenue is adjusted by multiplying expected revenue by the ratio of the actual price to the expected price (in CFA francs). This is calculated on a quarterly basis.

21. If the basic primary budget surplus exceeds the quantitative program indicator (2a) and/or if additional nonearmarked budgetary support, over and above the program amount, becomes available, the authorities will use these extra resources to

- finance the residual budgetary gap;
- further reduce external payment arrears on debt not eligible for rescheduling; and/or
- reduce the net claims of the banking system on the government (excluding the counterpart use of Fund resources).

IV. STRUCTURAL INDICATORS

22. The structural indicators are laid out in Table 7 of the memorandum on economic and financial policies.

23. The certification of oil revenues by an external auditor, based on the terms of reference of the certification for the third quarter of 2003, will include, *inter alia*, (i) verification of the tax declarations of the oil companies, (including compliance with the terms of production-sharing contracts—CPPs), (ii) reconciliation of the commercial transactions of the national oil company (SNPC) and the quantity of oil due to the government in settlement of the oil companies' tax liabilities (the SNPC included), and (iii) verification that the corresponding revenue has been transferred to the treasury.

24. The government's adoption of an action plan for implementing all the recommendations of the SNPC audit will be articulated in a letter addressed to the IMF Managing Director by the supervisory ministers, namely, the Minister of Economy, Finance, and Budget and the Minister of Hydrocarbons; a copy of the action plan will be attached thereto.

25. The government's adoption of a policy on the payment of dividends by the SNPC will be done by the supervisory ministers, namely, the Minister of Finance and the Minister of Hydrocarbons. An independent expert on the Organization for the Harmonization of Business Law in Africa (OHADA) matters will issue a legal opinion that the policy is consistent with the laws of the Republic of Congo and the rules and regulations applicable to the SNPC.

26. Work on the SNPC audit for fiscal-year (FY) 2002 is scheduled to begin no later than mid-May 2004, with a view to having the final report produced by end-July. For FY 2003, FY 2004, and FY 2005, a different contract from the one in effect for FY 2002 will be awarded by end-August 2004, with the terms of reference specifying that the auditors should submit their final reports for each fiscal year within two months after the SNPC produces its consolidated accounts. Furthermore, the authorities intend to request that the SNPC accelerate production of the consolidated accounts to meet the following deadlines: for FY 2003, by end-December 2004; for FY 2004, by end-November 2005; and for FY 2005, by end-October 2006.

27. The call for bids for the 2002 financial audit of the national oil refinery (CORAFA) is scheduled for no later than April 15, 2004, and the contract is to be signed by August 31. In that case, work will start by September 15, and the final report will be submitted to the Ministry of Finance no later than December 15, 2004.

28. The consolidated provisional balance sheet of the treasury for January 2004, produced in March 2004, must show an opening and closing balance, as well as the details of activity for the period.

29. The privatization of the CAIC bank will be considered complete once all the capital of the new bank (La Congolaise des Banques) that will replace it is released and the new bank becomes operational.

V. INFORMATION FOR PROGRAM MONITORING

A. Oil Sector

30. The government will submit the following information to the staff of the International Monetary Fund:

- monthly data on oil production by oilfield, production costs, volume exported, export prices, and the operations of the SNPC;
- the breakdown of the share of crude oil that accrues to the government by oil well, distinguishing the type of taxation to which this share is submitted (royalties, “profit oil”);
- any change in the tax parameters; and
- a breakdown of tax prices.

B. Government Finance

31. The government will submit the following information to the staff of the International Monetary Fund:

- A monthly table on government fiscal operations (TOFE) and its annexes; these data will be submitted monthly within four weeks after the end of the month. The annexed tables include the breakdown of oil revenue in value terms with the corresponding notes on computation, “excess oil” trends and any bonus payments, the breakdown of tax and nontax revenue, and the breakdown of central government expenditure, particularly transfers and common expenses.
- The monthly data on prices and taxation of petroleum products. These data will include (i) the price structure in effect during the month; (ii) the details of computation of the price structure, of the f.o.b. Mediterranean price at retail prices; (iii) amounts released

for sale; and (iv) a breakdown of the tax revenue from oil products—customs duties and value-added tax (VAT)—and direct/indirect subsidies supported by the budget. These data are transmitted within four weeks after the end of the month.

- Data on implementation of the public investment program, including the breakdown of financing sources. If the data on the execution of investments financed with foreign grants and loans are not available on schedule, a linear estimate of execution in comparison with annual forecasts will be used. These data (preliminary for bank credit) will be reported on a quarterly basis within four weeks after the end of the quarter.
- Complete monthly data on domestic financing of the budget (net bank credit and net nonbank funding of the government). These data will be reported monthly within four weeks after the end of the month.

C. Monetary Sector

32. The government will submit on a monthly basis, within four weeks of the end of the month the following preliminary information:

- data on net bank credit to the government/net domestic financing of the government;
- the consolidated balance sheet of the monetary institutions, central bank, and commercial bank surveys;
- the provisional integrated monetary survey;
- lending and deposit rates; and
- the usual banking supervision indicators for banks and nonbank financial institutions, where necessary.

The final data on the monetary survey will be provided within six weeks of the end of the month.

D. Balance of Payments

33. The government will submit the following to the staff of the IMF:

- any revised balance of payments data (including services, private transfers, official transfers, and capital and financial account transactions) as soon as the data are revised;
- foreign trade statistics (volume and price) prepared by the national statistics agency/BEAC, within three months after the end of the reporting month; and

- the preliminary annual balance of payments data, within nine months after the end of the reference year.

E. Debt

34. The government will submit the following to the staff of the IMF within four weeks of the end of the month:

- data on the stock, accumulation, and payment of domestic arrears;
- data on the stock, accumulation, and payment of external payment arrears;
- a breakdown of estimated domestic and external debt service, service due, and actual payments, including breakdowns of principal and interest and by creditor;
- the list and amounts of new external debt incurred or guaranteed by the government, with detailed information on the terms and conditions (currency, interest rate, grace period, and maturity) stated in the original agreement; and
- actual disbursements of foreign financial assistance (project and nonproject), including new borrowing and any external debt relief granted by foreign creditors (CCA tables).

F. Real Sector

35. The government will submit the following to the staff of the IMF:

- monthly itemized consumer price indices, on a monthly basis, within four weeks of the end of the month;
- provisional national accounts within nine months of the end of the year;
- any revision of the national accounts; and
- any other indicators and statistical data used to track overall economic developments, including information on activity in the forestry sector and wood-processing industry, as well as the monthly short-term economic bulletins prepared.

G. Structural Reforms and Other Information

36. The government will submit the following information:

- any study or official report on the economy of the Republic of Congo, within two weeks of its publication; and

- any decision, order, law, decree, ordinance, or circular having economic or financial implications, within two weeks from the time it is published or, at the latest, from its entry into force.

REPUBLIC OF CONGO: PUBLIC DEBT SUSTAINABILITY ANALYSIS

The analysis shows that an unsustainable debt burden would persist into the medium term even under the assumption of sound policies and the application of full traditional debt relief mechanisms. The Congo is extremely vulnerable to adverse shocks.

1. The baseline projections assume the implementation of sound macroeconomic policies. Oil production is projected to increase steadily until 2010 when it plateaus at 110 million barrels per year (compared to 84 million barrels in 2004) for the remainder of the projection period. Nonoil real GDP is projected to grow at an average of close to 5 percent per year, initially on the basis of strong growth in the forestry sector (as current investments come online) and later in mining and public utilities (as security allows exploration and public investments come onstream). The current account surplus is projected to rise to about 1 percent of GDP by 2010, primarily due to the increases in oil exports, but over the longer term, it is projected to be roughly balanced. In the fiscal area, the overall budget balance is projected to become positive by 2009 on the basis of higher oil revenues and slightly lower primary current expenditures. Nonoil revenue is projected to rise steadily to about 20 percent of nonoil GDP by 2010 (from around 18 percent in 2004), and the composition of public expenditures is expected to shift in favor of capital outlays over the long term.
2. On external debt, the baseline assumes no debt relief and no settlement of external arrears. Additionally, new arrears are accumulated on potentially reschedulable debt service,¹ late interest on the stock of arrears accrues at market rates, and all new borrowing (including on financing gaps) is on commercial terms. Under this scenario, the Congo's external debt to GDP ratio would remain unsustainable into the long-term with NPV of debt to GDP remaining in excess of 150 percent by the end of the projection period, 2023 (Table 1). The debt sustainability indicators worsen slightly when domestic debt is taken into account in the analysis (Table 2). The results of the stress tests show that the Congo is vulnerable to external shocks, in particular to the decline in exports and GDP growth, and shortfalls in primary fiscal balance.
3. The alternative scenario assumes: (i) a hypothetical Paris Club stock-of-debt operation on Naples terms—67 percent NPV reduction on eligible debt, including arrears—and comparable treatment by other bilateral and commercial creditors; (ii) settlement of external arrears at end-2003; and (iii) new borrowing on IDA terms.² Although the

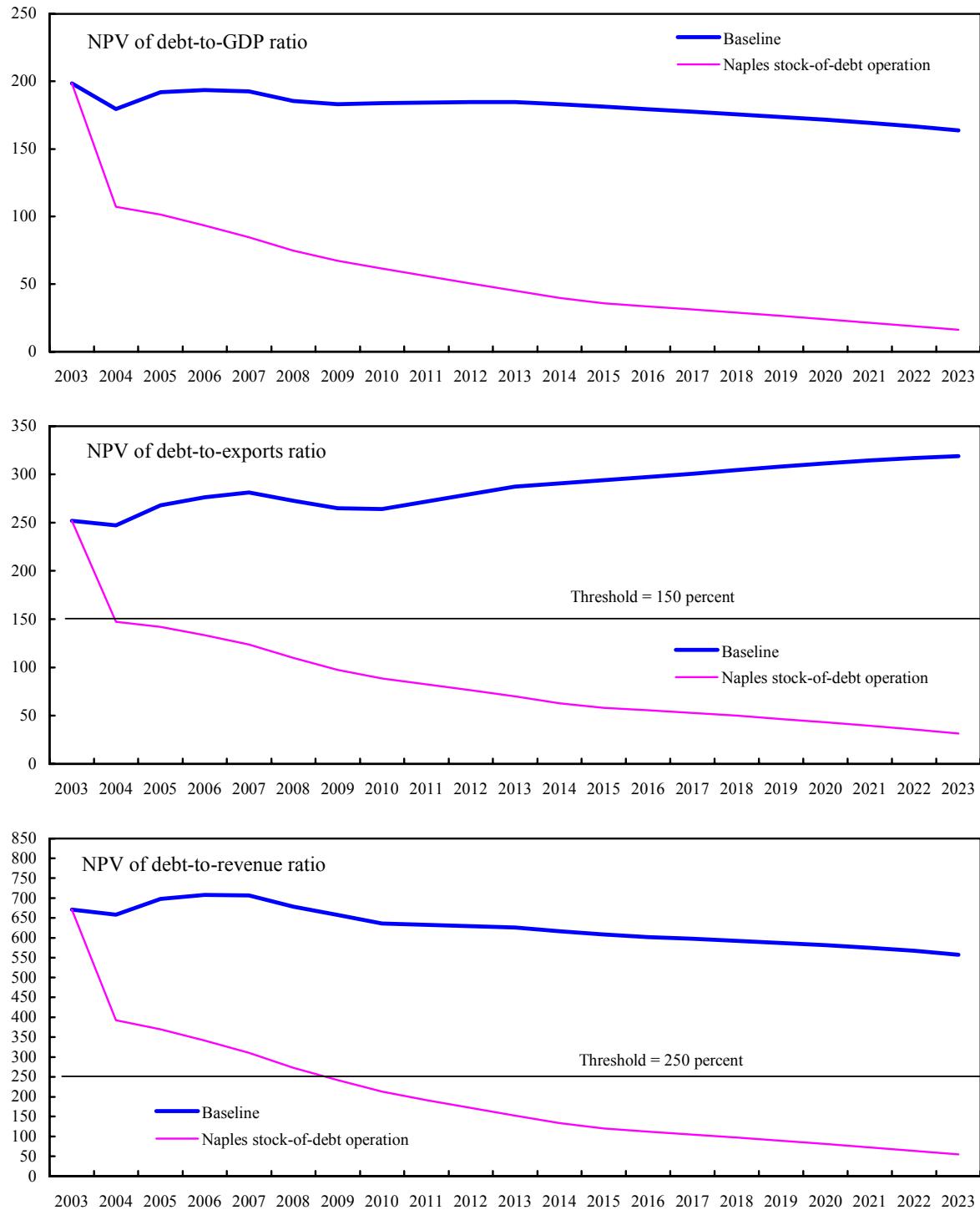
¹ Debt service due to Paris Club creditors on pre-cutoff-date debt, and to other bilateral and private creditors (excluding debt service on oil-collateralized debt). The creditors of oil-collateralized loans have a legally-binding and direct claim on Congo's oil shipment as collateral.

² It is assumed that half of the financing gap is covered by new concessional borrowings and the remaining by grants.

application of debt relief induces a significant improvement in the debt indicators (Table 3), the Congo's debt would remain unsustainable over the medium term: the key criterion, NPV of debt-government revenue ratio,³ remains above the 250 percent threshold into 2008.

³ As a very open economy, the Congo would qualify for debt relief under the fiscal window.

Figure 1. Republic of Congo: Indicators of Public and Publicly Guaranteed External Debt, 2003–23
(In percent)



Source: Staff projections and simulations.

Table 1. Republic of Congo: Sensitivity Analysis of External Public Debt, 2003-23
(In percent)

	Estimate	Projections						
		2003	2004	2005	2006	2007	2008	2013
NPV of debt-to-GDP ratio								
Baseline	199	180	192	194	193	185	185	164
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2004-23 1/	199	210	221	230	237	242	262	290
A2. New public sector loans on less favorable terms in 2004-23 2/	199	180	193	195	194	187	186	166
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2004-05	199	191	216	218	217	209	208	185
B2. Export value growth at historical average minus one standard deviation in 2004-05 3/	199	194	225	228	225	215	200	165
B3. US dollar GDP deflator at historical average minus one standard deviation in 2004-05	199	246	306	309	307	296	294	261
B4. Net non-debt creating flows at historical average minus one standard deviation in 2004-05 4/	199	188	209	211	209	200	192	164
B5. Combination of B1-B4 using one-half standard deviation shocks	199	237	280	282	280	268	261	225
B6. One-time 30 percent nominal depreciation relative to the baseline in 2004 5/	199	246	263	266	264	254	253	225
NPV of debt-to-exports ratio								
Baseline	252	242	268	277	281	273	286	317
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2004-23 1/	252	282	308	328	345	356	406	561
A2. New public sector loans on less favorable terms in 2004-23 2/	252	242	269	278	283	275	289	321
B. Bound Tests								
B1. Export value growth at historical average minus one standard deviation in 2004-05 3/	252	324	422	437	441	424	416	429
B2. Net non-debt creating flows at historical average minus one standard deviation in 2004-05 4/	252	253	291	301	305	294	298	318
B3. Combination of B1-B4 using one-half standard deviation shocks	252	277	300	311	314	304	311	335
Debt service ratio								
Baseline	18	24	27	22	21	21	16	14
A. Alternative Scenarios								
A1. Key variables at their historical averages in 2004-23 1/	18	27	29	25	26	28	27	27
A2. New public sector loans on less favorable terms in 2004-23 2/	18	24	27	22	21	21	16	14
B. Bound Tests								
B1. Real GDP growth at historical average minus one standard deviation in 2004-05	18	24	27	22	21	21	16	14
B2. Export value growth at historical average minus one standard deviation in 2004-05 3/	18	30	37	33	34	36	29	19
B3. US dollar GDP deflator at historical average minus one standard deviation in 2004-05	18	24	27	22	21	21	16	14
B4. Net non-debt creating flows at historical average minus one standard deviation in 2004-05 4/	18	24	27	23	23	24	19	14
B5. Combination of B1-B4 using one-half standard deviation shocks	18	26	29	24	24	24	19	15
B6. One-time 30 percent nominal depreciation relative to the baseline in 2004 5/	18	24	27	22	21	21	16	14
<i>Memorandum item:</i>								
Grant element assumed on residual financing (i.e., financing required above baseline)	1	1	1	1	1	1	1	1

Source: Staff projections and simulations.

1/ Variables include real GDP growth, growth of GDP deflator (in U.S. dollar terms), non-interest current account in percent of GDP, and non-debt creating flows.

2/ Assumes that the interest rate on new borrowing is 2 percentage points higher than in the baseline, while grace and maturity periods are the same as in the baseline.

3/ Export values are assumed to remain permanently at the lower level, but the current account as a share of GDP is assumed to return to its baseline level after the shock (implicitly an offsetting adjustment in import levels).

4/ Includes official and private transfers and FDI.

5/ Depreciation is defined as the percentage decline in dollar/local currency rate, such that it never exceeds 100 percent.

6/ Applies to all stress scenarios except for A2 (less favorable financing) in which the terms on all new financing are as specified in footnote 2.

Table 2. Republic of Congo: Sensitivity Analysis of Public Sector Debt, 2003-2023 1/

	Estimate 2003	Projections						
		2004	2005	2006	2007	2008	2013	2023
NPV of Debt-to-GDP Ratio								
Baseline	212	202	210	210	207	198	190	162
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	212	208	221	226	228	229	252	299
A2. Primary balance is unchanged from 2003	212	200	204	200	193	181	161	112
B. Bound tests								
B1. Real GDP growth is at baseline minus one standard deviations in 2004-2005	212	212	231	233	232	225	229	223
B2. Primary balance is at baseline minus one standard deviations in 2004-2005	212	207	220	220	217	208	201	173
B3. Combination of 2-3 using one half standard deviation shocks	212	209	224	224	221	211	204	177
B4. Long-run real GDP growth is at baseline minus one standard deviations	212	204	215	217	217	210	223	254
B5. One time 30 percent real depreciation in 2004	212	291	301	300	294	280	263	214
B6. 10 percent of GDP increase in other debt-creating flows in 2004	212	212	221	221	218	208	201	173
NPV of Debt-to-Revenue Ratio 2/								
Baseline	706	719	750	755	747	712	631	542
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	706	739	788	810	822	823	834	992
A2. Primary balance is unchanged from 2003	706	711	730	719	697	653	536	375
B. Bound tests								
B1. Real GDP growth is at baseline minus one standard deviations in 2004-2005	706	751	824	837	837	807	760	745
B2. Primary balance is at baseline minus one standard deviations in 2004-2005	706	736	787	792	785	749	667	578
B3. Combination of 2-3 using one half standard deviation shocks	706	742	799	804	797	761	678	590
B4. Long-run real GDP growth is at baseline minus one standard deviations	706	726	766	780	782	757	739	848
B5. One time 30 percent real depreciation in 2004	706	1036	1077	1077	1061	1009	874	714
B6. 10 percent of GDP increase in other debt-creating flows in 2004	706	754	788	793	786	750	669	579
Debt Service-to-Revenue Ratio 2/								
Baseline	53	48	52	37	32	29	15	6
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	53	49	54	39	35	34	23	31
A2. Primary balance is unchanged from 2003	53	48	51	36	29	25	5	-13
B. Bound tests								
B1. Real GDP growth is at baseline minus one standard deviations in 2004-2005	53	50	56	40	35	33	23	25
B2. Primary balance is at baseline minus one standard deviations in 2004-2005	53	48	52	38	35	33	19	11
B3. Combination of 2-3 using one half standard deviation shocks	53	49	54	39	34	32	18	10
B4. Long-run real GDP growth is at baseline minus one standard deviations	53	48	52	38	33	30	20	28
B5. One time 30 percent real depreciation in 2004	53	51	57	42	37	33	20	13
B6. 10 percent of GDP increase in other debt-creating flows in 2004	53	48	53	38	36	33	19	11

Table 2. Republic of Congo: Sensitivity Analysis of Public Sector Debt, 2003-2023 (concluded) 1/

	Estimate 2003	Projections						
		2004	2005	2006	2007	2008	2013	2023
Debt Service-to-GDP Ratio								
Baseline	16	13	14	10	9	8	4	2
A. Alternative scenarios								
A1. Real GDP growth and primary balance are at historical averages	16	14	15	11	10	9	7	9
A2. Primary balance is unchanged from 2003	16	13	14	10	8	7	1	-4
B. Bound tests								
B1. Real GDP growth is at baseline minus one standard deviations in 2004-2005	16	14	16	11	10	9	7	8
B2. Primary balance is at baseline minus one standard deviations in 2004-2005	16	13	15	11	10	9	6	3
B3. Combination of 2-3 using one half standard deviation shocks	16	14	15	11	10	9	5	3
B4. Long-run real GDP growth is at baseline minus one standard deviations	16	14	15	10	9	8	6	8
B5. One time 30 percent real depreciation in 2004	16	14	16	12	10	9	6	4
B6. 10 percent of GDP increase in other debt-creating flows in 2004	16	13	15	11	10	9	6	3

Sources: Congolese authorities; and Fund staff estimates and projections.

1/ Includes domestic and external public debt. Average exchange rates were used in the external DSA for GDP computation, hence the differences between the two DSAs on external debt ratios.

2/ Revenues are defined inclusive of grants.

Table 3. Republic of Congo: External Debt Sustainability Indicators, 2003–2023 1/
(In percent, unless otherwise indicated)

	Actual 2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2023	Averages 2004-2013 2014-2023
No arrears clearance (baseline scenario)															
NPV of debt to GDP ratio	199	180	192	194	193	185	183	184	184	185	185	183	181	164	186
NPV of debt to exports ratio	252	247	268	276	281	273	265	264	272	280	287	291	294	319	174
NPV of debt to revenue ratio 2/	671	658	698	708	707	678	658	636	633	629	626	617	608	557	306
Debt service to exports ratio	18	24	27	22	21	21	19	15	15	15	16	15	14	20	588
Debt service to revenue ratio 2/	48	65	70	56	53	51	48	37	36	35	34	33	32	24	15
After full traditional debt relief (scenario 2)															
NPV of debt to GDP ratio	199	107	102	93	85	75	67	62	56	50	45	40	36	16	74
NPV of debt to exports ratio	252	147	142	133	124	110	97	88	82	76	70	63	58	32	48
NPV of debt to revenue ratio 2/	671	392	370	341	311	273	242	213	192	172	153	134	120	55	93
Debt service to exports ratio	18	18	23	17	15	14	12	11	10	10	10	9	6	5	266
Debt service to revenue ratio 2/	48	48	59	42	39	34	31	26	24	23	21	20	13	8	14
Memorandum items:															
GDP	3516	4029	3938	4076	4272	4584	4801	4961	5132	5320	5527	5793	6081	9334	4664
Exports of goods and services	2772	2927	2820	2836	2925	3120	3319	3453	3480	3513	3553	3649	3750	4197	7390
Government revenue 2/	1040	1100	1082	1115	1164	1254	1337	1433	1496	1562	1631	1720	1812	2743	4178
														1317	2185

Source : Congolese authorities; and staff estimates and projections.

1/ All debt indicators refer to public and publicly guaranteed (PPG) debt.

2/ Revenue is defined as central government revenue excluding grants.

Bank of the Central African States: Safeguards Assessment

Introduction

The Bank of the Central African States (BEAC) is the common central bank of the Central African States, which includes the Republic of Congo. A Stage Two (on site) safeguards assessment of the BEAC was completed in July 2001 and proposed specific remedies to alleviate vulnerabilities that were identified by staff. The authorities have committed to implement most of the proposed remedies, as described in the following sections.

Safeguards areas and main remedies

The external audit mechanism: The auditing function and the quality control procedures of the external auditor are adequate. The safeguards assessment proposed that: (i) the external auditor refer explicitly to the international standards of auditing (ISA) in its opinion, (ii) the external auditor become more cognizant of the accounting rules applicable to the recording of Fund's balances; and (iii) the BEAC should include the audit opinion in the annual publication of the financial statements. The management of the BEAC has agreed to implement these actions for the FY 2002 accounts.

Legal structure and independence: The legislation governing BEAC is adequate.

Financial reporting: The monthly statements of the bank's financial position are not published in any form and the December 31, 2000 audited financial statements were not published in a timely manner. The staff recommended that the BEAC: (i) enhance the readability and the credibility of the published annual accounts by including detailed explanatory notes on the accounting methods followed, and if these methods referred explicitly to a generally accepted accounting framework; (ii) adopt International Accounting Standards; and (iii) change the accounting of some of its operations with the Fund, especially with regard to the revaluation of the IMF accounts. The management of the BEAC has agreed to implement these recommendations by FY 2002.

Internal audit mechanism: The quality of the personnel, the rigorous methods followed for the audit of branches, the training program in place, and the risk assessment methods in place are satisfactory. However, certain weaknesses remain and staff recommended that the BEAC: (i) establish a charter for the Internal Audit Department (IAD); (ii) expand the audit scope and coverage of IAD to include activities at headquarters; (iii) prepare an annual rolling multi-year audit program describing risk assessment, activities scheduled, staffing and financial resources required, and (iv) increase the number of qualified staff.

In its response to the Stage Two report, the management of the BEAC has specifically agreed to expand the scope and coverage of the audit department, and increase the number of qualified staff. A charter for the audit department will also be prepared, with the assistance of

Fund staff, which will provide the BEAC with the relevant documentation. A gradual implementation of these recommendations should be completed by end 2002. The management of the BEAC did not specifically cover in its answer to the report the recommendation related to the risk-based rolling multi-year audit program.

The system of internal controls: On the whole, the risks are relatively well captured, although uncertainties exist because of insufficient a posteriori controls exercised on some activities at headquarters. The bank has a codified system of rules, selects its personnel carefully, maintains segregation of duties in the branches, and has recently increased resources for control purposes. Nevertheless, the staff recommended that BEAC: (i) strengthen the coordination among the audit bodies; (ii) examine in depth the segregation of duties at headquarters; and (iii) put in place a more systematic follow-up of all recommendations made by the external auditor to allow the Governor and the Board of Directors to better exercise their oversight responsibilities.

In its response to the Stage Two report, the management of the BEAC has agreed to establish an audit committee by 2002. Regarding the proposed segregation of duties, management noted that an internal assessment was under way, but that for budgetary reasons a formal audit cannot be undertaken before end-2002.

Regarding late payments of Fund obligations, which was an issue for all of the BEAC's member countries at some time in the last three years, the staff concluded that, while the BEAC's own payment procedures and related management controls in this area are functioning adequately, procedures should be modified with respect to BEAC's relations with member countries. The staff recommended that the BEAC should repay the Fund directly using its own resources for those countries with borrowing capacity with the central bank; for countries facing fiscal difficulties, staff recommended that they at least maintain sufficient borrowing capacity with the BEAC to repay IMF obligations falling due within the next year. In its answer to the Stage Two Report, the management of the BEAC did not follow the mission's recommendation that the BEAC should repay the Fund directly. The management also commented that apart from direct statutory advances to Treasuries, the BEAC could not grant loans to member countries.

Republic of Congo: Statistical Issues

1. The Republic of Congo's statistical infrastructure is being slowly rebuilt after the civil strife of 1997 and December 1998–October 1999, during which severe damage on administrative infrastructure was inflicted and many records were lost. The current coverage of the Congo's statistics is described below. Social statistics are weak. Since October 2001, a resident statistical expert has been assisting the authorities with the macroeconomic statistics.
2. A multisector mission that visited Brazzaville in May 2002 prepared a diagnostic of the statistical system. The mission's general conclusion was that the Congo's macroeconomic statistics are weak and suffer from the absence of a national statistical program, and shortages of financial, physical, and human resources. It recommended measures for improvement, which are being followed up by the statistical advisor.
3. The Republic of Congo is a participant in the General Data Dissemination System (GDDS), and its metadata were posted on the Fund's Dissemination Standards Bulletin Board (DSBB) on November 5, 2003.

National accounts

4. The quality of national accounts data is weak. The compiled data show inconsistencies, both internally and with the balance of payments. Estimates for the informal sector are based on information that dates back to 1978. The authorities provide Fund missions with a breakdown of GDP by expenditures and sectors, both in nominal and real terms. These data are prepared by the Directorate General of Statistics (DGS) of the Ministry of Finance. Historically, data on oil sector transactions have been weak, reflecting a lack of transparency on the part of the oil companies operating in the country and the government agencies dealing with them.

Employment and unemployment

5. Annual data on employment in the central government are available from the Ministry of Finance, but they are not consistent with data from the civil service roster of the Ministry of the Civil Service. As part of the structural reforms undertaken in the context of the post-conflict program, the government completed an audit of public service employees and established a new civil service payroll roster. Data on employment in the private sector are not available.

Prices

6. Movements in the prices of commodities consumed by households are recorded for the capital city of Brazzaville (weights for 1977 and price reference period of December 1977) and the second-largest city of Pointe Noire (price reference period of January 1996 and weights for 1989). Weights no longer reflect current household consumption patterns. Data

are compiled on a monthly basis. The authorities intend to compile a CPI that is harmonized with other CEMAC countries.

Government accounts

7. Compilation of **government finance statistics** (GFS) is neither comprehensive nor systematic. The *Tableau des Opérations Financières de l'État* (TOFE) is based on several disparate sources rather than a comprehensive set of accounting statements. Financing data are currently obtained from money and banking data instead of the government accounts. As a result, intersectoral consistency between government finance and money and banking statistics cannot be ascertained, impeding the assessment of accuracy of these data.

8. At the time of the May 2002 multisector mission, the *Balance des comptes du Trésor*, a basic and essential treasury source document, as well as other sources, were not made available to the producers of the TOFE.¹⁶ The mission recommended that systematic procedures be established for the compilation of government finance statistics, based, to the extent possible, on a unified set of accounting and administrative records.

9. TOFE compilers do not have access to relevant financial statements of the Société Nationale des Pétroles Congolais (SNPC), which carries out several operations on behalf of the government (notably in the oil sector).

10. In 2003, the Congo reported GFS to STA for publication in the *GFS Yearbook* using the new *GFSM 2001* template. The Congo does not report subannual GFS data for publication in *IFS*. The compilation of GFS statistics to be reported to the Fund should be carried out in close cooperation with the compilers of the TOFE.

11. Progress is underway to address these shortcomings. In February/March 2003, a FAD follow-up mission found that most of the recommendations of the 2001 FAD mission on expenditure management, in particular with regard to the centralization of all government revenue and execution of public expenditure through the budget, are being implemented or are underway and steps have been taken to computerize the expenditure chain.

Monetary accounts

12. Monthly data on monetary statistics for the Congo, as well as for the other members of the Central African Economic and Monetary Community (CEMAC), are regularly reported to the Fund in electronic form by the regional central bank (BEAC). Accuracy of monetary data is affected by large cross-border movements of currency among CEMAC

¹⁶ This compilation is not undertaken on the basis of treasury accounting records, to which the compilers themselves do not have access. The mission examined the Excel worksheet used for the compilation of the TOFE and made recommendations for improvements, although it could not establish the links between that worksheet and the primary data sources.

member countries. However, the Congo is moderately affected by such movements: 7.5 percent of banknotes issued in the Congo by the BEAC national directorate circulate in Cameroon and about 3.5 percent in Gabon, while currency in circulation in the Congo includes about 6.5 percent of banknotes from Cameroon and about 3.5 percent from Gabon.

13. The monetary and financial statistics mission that visited the BEAC headquarters (May 2001) provided technical assistance on the compilation and timeliness of monetary statistics. The mission discussed an action plan for the implementation of the *Monetary and Financial Statistics Manual (MFSM)* and for the introduction of an area-wide page in *IFS* for the CEMAC. Following the 2001 mission, a regional workshop on monetary and financial statistics was organized by the BEAC in Libreville (Gabon) in May 2002 to support the implementation of the *MFSM* in the CEMAC countries. The new page for CEMAC was published in the January 2003 issue of *IFS*.

14. The May 2002 multisector mission found that the institutional coverage of government and of nonfinancial public sector in monetary statistics are outdated and need to be revised.

External and domestic debt

15. The Caisse Congolaise d'Amortissement (CCA) produces comprehensive data on the outstanding stock of external public debt, including arrears and its composition, together with detailed projections on debt service due. These data are provided to Fund missions. However, the debt-stock data cannot be reconciled with flow data in the balance of payments. The CCA also produces domestic debt data.

Balance of payments and trade statistics

16. As in other CEMAC countries, the national agency of the BEAC is responsible for the collection and the dissemination of balance of payments data in the Congo. The balance of payments statistics are prepared on an annual basis while the compilation system has been specifically designed to produce quarterly data. Through 1994, balance of payments data were compiled in the framework of the *Balance of Payments Manual, Fourth Edition*. The BEAC provides annual data on exports of goods and services and on capital flows other than public debt. Since 1995, data are being prepared using the *Balance of Payments Manual, Fifth Edition*. In 2003, balance of payments data for 1995 through 2002 were reported to the Fund for publication in *International Financial Statistics*.

17. In May 2002, the technical assistance mission found the compilation system and procedures for balance of payments statistics to be conceptually sound but flawed in their application due to the absence of documented sources and methods, understaffing, and lack of training. This situation has resulted in significant delays in the production of balance of payments statistics and, in general, poor monitoring of the quality of the input data provided by the statistical respondents. Furthermore, the opacity surrounding certain transactions in the oil sector introduces an important element of imprecision. In addition, net investment

flows are overestimated by significant unrecorded disinvestment operations that are part of the tax regime arrangements obtained by oil-drilling nonresident companies.

18. The Fund's resident expert on statistics, who took up his assignment at end-October 2001, has been assisting the authorities in developing an appropriate methodology for compiling balance of payments statistics. This resulted in improved data communication in 2003 and balance of payments detailed data were submitted for the period 1995–2002.

Public enterprise sector

19. There is no centralized, comprehensive database on the operations of public enterprises. However, some information has been made available to Fund missions by individual enterprises.

Republic of Congo: Core Statistical Indicators
(As of April 28, 2004)

Exchange Rates	International Reserves	Reserve/ Base Money	Central Bank Balance Sheet	Broad Money	Interest Rates	Consumer Price index	Exports and Imports	Current Account Balance	Overall Government Balance	National Accounts	External Debt
4/28/04	12/03	12/03	12/03	12/03	12/03	01/04	2003	2003	3/04	2003	3/04
Date received	4/28/04	3/04	3/04	3/04	3/04	03/04	2/04	2/04	4/04	2/04	4/04
Frequency of data 1/	D	M	M	M	M	O 2/	M	A	Q	A	M
Frequency of reporting 1/	D	M	M	M	M	O 2/	M	A	Q	A	M
Source of data 3/	N	A	A	A	A	A	C	V	V	A	A
Mode of reporting 4/	O 5/	E	E	E	E	C	C	V	C	V	V
Confidentiality 6/	C	A	A	A	A	A	A	A	A	A	A
Frequency of publication 1/	D	M	M	M	M	M	A	A	Q	A	A

1/ Frequency of data, reporting, and publication: D=daily, W=weekly, M=Monthly, Q=quarterly, or A=annually.

2/ Information communicated to staff as adjustments in interest rates occur.

3/ Source of data: A=direct reporting by Central Bank, Ministry of Finance, or other official agency, or N=official publication or press release.

4/ Mode of reporting: E=electronic data transfer, C=cable or facsimile, T=telephone, M=mail, V=staff visits, or O=other.

5/ As reported in the daily morning press (euro exchange rate).

6/ Confidentiality: A=for use by staff only, B=for use by the staff and the Executive Board, or C=for unrestricted use.

Statement by the IMF Staff Representative
June 10, 2004

1. This supplement contains information on recent economic developments in the Republic of Congo since the circulation of the staff report for the 2004 Article IV consultation and new staff-monitored program. The information does not alter the thrust of the staff appraisal.

2. The implementation of the staff-monitored program (SMP) was broadly satisfactory through end-April (see Appendix III of the staff report for the details of the SMP).

- All end-March quantitative targets were met. In particular, the primary fiscal balance was met by a comfortable margin owing to higher-than-projected non-oil revenues and enhanced expenditure control. No new domestic arrears were accumulated. In addition, external debt service payments due to multilateral institutions and Paris Club creditors on post-cutoff-date debt were made on a timely basis and the ceiling on domestic arrears payments was respected.
- Most structural targets were met. Particularly noteworthy were the external certification of oil revenues in 2003 and the adoption of an action plan for the reform of the accounts and operations of the national oil company (SNPC), as well as publication on an internet site (www.congo-site.cg) of the above-mentioned SNPC action plan, the reports from the oil revenue certification, and parts of the 1999–2001 audit of the SNPC. However, three structural measures were only partially implemented. First, not all of the production sharing agreements (PSAs) with oil companies already published in the official gazette were posted on the internet. Second, the information published on financial transactions carried out by the SNPC on behalf of the government in 2002–03 was incomplete, especially with respect to interest costs and commissions. Third, while significant progress has been made in centralizing revenues at the treasury, forestry tax revenues (which represent about 6 percent of non-oil revenues) have yet to be transferred to the treasury. The government plans to rapidly take corrective actions on all these measures.

3. On the basis of the broadly satisfactory implementation of the SMP through end-April, the staff initiated negotiations in May 2004 on a program that could potentially be supported by a new three-year arrangement under the Poverty Reduction and Growth Facility (PRGF). The conclusion of these negotiations with a recommendation in support of such a new arrangement would be conditional on (i) continued good implementation under the SMP through end-June 2004, (ii) completion of all the SMP structural measures, (iii) implementation of possible prior actions to be determined in the course of the PRGF negotiations, and (iv) obtaining full financing assurances. In addition, staff would need to have adequate information on the 2003 financial settlement between the government and an international oil company.



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IMF Concludes Article IV Consultation with the Republic of Congo

On June 10, 2004, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with the Republic of Congo.¹

Background

The gradual reestablishment of political stability and democratic institutions over the past four years has generated a sense of guarded optimism that the Congo is on the cusp of a structural break from the previous pattern of intermittent outbreaks of civil conflict. Over the past year, security improvements have been consolidated by the launch of the demobilization program for former combatants, and further progress has been registered with respect to the reestablishment of democratic institutions.

In the context of improved security, the pace of economic activity in the non-oil sector has increased (particularly in agriculture, commerce, and transportation). Non-oil real GDP increased by about 10 percent per annum on average during 2000–03. Consumer price inflation decelerated significantly in the postwar period, helped by a more reliable supply line from Pointe-Noire to Brazzaville and a strengthening of the euro.

Nonetheless, key social indicators have continued to deteriorate, and the external debt burden is heavy.

¹ Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities.

The fiscal position in 2003 improved from the exceptionally poor performance of 2002, but the underlying fiscal effort was weak relative to the 2003 budget. Higher-than-budgeted oil revenue, together with lower-than-budgeted investment and interest expenditures, generated an improvement in the overall fiscal balance to 0.4 percent of GDP in 2003 (from -8.1 percent in 2002). However, effective budget execution was hampered by weaknesses in expenditure controls, ineffectual treasury management, and delays in the implementation of non-oil revenue measures. A significant amount of windfall oil revenue was used to pay unbudgeted domestic commercial arrears. Steps were taken later in 2003 to start correcting these deficiencies.

In an encouraging sign of a pickup in non-oil sector activity, credit to the economy grew in 2003 at a faster rate than non-oil GDP for the first time in three years. Nonetheless, bank deposits decreased by 8 percent in 2003, partly in response to the difficulties in effecting current transfers. The recent privatization of the last remaining state-owned bank, Crédit pour l'Agriculture, l'Industrie et le Commerce (CAIC), in early 2004, coupled with the expected continued improvement in non-oil sector activity, should strengthen confidence in the banking sector.

The external current account remained relatively unchanged, with a surplus of 0.3 percent of GDP registered in 2003. The decline in oil export value, owing to a contraction in production that was only partially offset by higher prices, was offset by lower government imports and interest due on external debt. The authorities made efforts in 2003 to start normalizing relations with external creditors by (i) remaining current on debt-service payments to multilateral and Paris Club creditors (with the exception of one bilateral creditor), and (ii) clearing arrears to a few multilateral creditors. The Congo remains a heavily indebted country, with an external debt stock equivalent to about 185 percent of GDP at end-2003, two-thirds of which represents arrears.

On the structural front, performance was mixed in 2003. The audit of the SNPC for fiscal years 1999-2001 was completed, efforts were made to centralize government revenues, no new oil-collateralized debt was contracted, and initiatives were launched to publish oil sector data. Nonetheless, the privatization of the remaining publicly owned bank (CAIC) was delayed, and the end-September 2003 measures on oil sector transparency were not implemented. In the last quarter of 2003, a significant step was taken to enhance transparency in the oil sector with the completion of the certification by an external auditor of government oil revenue for 2003.

Executive Board Assessment

Executive Directors welcomed the progress toward political stability in the Republic of Congo as well as the improvements in security. Directors commended the authorities for the strengthening of the macroeconomic situation, marked by strong growth in economic activity, including in the non-oil sector, and the easing of inflationary pressures. They noted, however, that the fiscal outturn in 2003 was weak compared with the budget, notwithstanding some improvement relative to 2002, that key social indicators have continued to deteriorate, and that the external debt burden remains heavy. Building on recent positive steps aimed at ensuring that the Congo's resources are effectively harnessed for the benefit of all its people, Directors encouraged the government to broaden ownership of the reform program further and to press ahead with crucial reform measures in order to lay the basis for sustained growth and poverty reduction.

Directors expressed concern about the considerable shortfalls in economic performance in 2003 vis-à-vis the objectives embedded in the staff-monitored program (SMP). Most Directors considered that the opportunity provided by favorable oil market developments could have been used more effectively to reduce external arrears and normalize relations with the international community. A few Directors supported the authorities' decision to use part of the oil windfall to clear some domestic arrears. Directors welcomed the progress made in advancing structural reforms in some areas. However, they felt that more could have been done in implementing reforms in key areas, including oil sector transparency and the privatization of a publicly-owned commercial bank. They also expressed concern over the accrual of new external arrears that cannot be re-scheduled, and urged the authorities to remain current on amounts falling due to multilateral creditors and on Paris Club post cut-off debt claims.

Directors stressed the need to improve fiscal management and adopt a more comprehensive medium-term framework, particularly in light of the formidable challenges posed by the heavy reliance on oil revenues. They also stressed the importance of strengthening non-oil revenue collection, including by reducing the widespread use of ad hoc tax and customs exemptions, and by centralizing revenue collection at the treasury. On the expenditure side, Directors urged the authorities to increase poverty-related spending, which would require reducing unproductive transfers and carefully selecting investment projects. They welcomed the authorities' intention to adopt a fiscal rule to project oil revenues and to program expenditures based on conservative oil price projections, and highlighted the need for complementary measures to ensure that any windfall revenues are used in a clear and transparent manner.

Directors noted the importance of creating an environment favorable to private sector business and investment activity in order to promote economic diversification. They stressed the need to prevent further erosion in the competitiveness of the non-oil sector. In this context, Directors urged the authorities to exercise vigilance on the fiscal front and to take steps to reduce the high costs of doing business in the Congo.

Directors welcomed recent efforts to enhance transparency in the oil sector. They commended the authorities for the completion of the external audit of the national oil company (SNPC), covering the fiscal years 1999-2001; the external certification of oil revenues in 2003; and the publication of key oil sector data on the internet. Nevertheless, Directors noted that the audit of the SNPC had revealed weaknesses in management and accounting practices as well as severe limitations in access to information, and they urged the authorities to improve the auditors' access to information for the 2002 audit. Directors urged timely implementation of the action plan adopted by SNPC so that future audits may provide a more accurate picture of the company's financial operations. They also encouraged the authorities to continue to publish the production sharing agreements between the government and the oil companies.

Directors encouraged the authorities to press ahead with their structural reform agenda. In particular, they stressed the need to strengthen governance and the rule of law, and welcomed the preparation of the anticorruption program. Directors recommended addressing issues of property rights, including establishing a land title system. They urged renewed efforts to

restructure the large public enterprises, particularly those expected to provide essential services. Directors welcomed the recent privatization of the remaining publicly-owned commercial bank, but noted that further efforts were needed to strengthen the financial sector. To allow commercial banks to play a more effective role in economic development, they noted that it was essential to address structural impediments to commercial bank lending to the private sector, in particular the weaknesses in the legal framework. Directors also called for forceful implementation of the regional framework on laws to prevent money laundering and the financing of terrorism.

Looking forward, Directors welcomed the authorities' renewed determination to establish a track record of policy performance including maintaining orderly relations with external creditors that could allow the Congo to move to a Fund-supported program. They were encouraged by the satisfactory results in the first quarter of 2004 under the six-month SMP. To ensure the support of the international community, including for possible debt relief, Directors stressed that enhanced public access to oil sector information should be a key aspect of a strategy to broaden ownership of the reform program, lower the probability of future conflicts, and enhance accountability. To this end, they emphasized the need for full transparency on all oil-related transactions. They welcomed the authorities' decision to participate in the Extractive Industries Transparency Initiative (EITI).

Directors encouraged the authorities to finalize preparation of the interim poverty reduction strategy paper (I-PRSP), implement a functional budget classification system to help monitor poverty-related outlays, and carry out the poverty-related surveys necessary to improve the social database.

Directors welcomed ongoing improvements of the statistical database, including the recent decision to participate in the IMF's General Data Dissemination System and the budgetary increases for statistical development. They urged the authorities to continue to expand further the coverage of the national statistics, including with respect to the coverage of the oil sector and poverty monitoring, and to make full use of the technical assistance from the Fund and other development partners.

Public Information Notices (PINs) form part of the IMF's efforts to promote transparency of the IMF's views and analysis of economic developments and policies. With the consent of the country (or countries) concerned, PINs are issued after Executive Board discussions of Article IV consultations with member countries, of its surveillance of developments at the regional level, of post-program monitoring, and of ex post assessments of member countries with longer-term program engagements. PINs are also issued after Executive Board discussions of general policy matters, unless otherwise decided by the Executive Board in a particular case.

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Republic of Congo: Selected Economic and Financial Indicators, 2001–03

	2001	2002	2003
(Annual changes in percent)			
Domestic economy			
GDP at constant prices	3.6	3.5	1.0
Oil	-7.5	-1.5	-7.2
Non-oil	12.1	6.7	5.8
GDP deflator	-13.9	-0.6	-3.9
Consumer prices (period average)	0.8	3.1	1.2
(In percent of GDP)			
Gross national savings	23.3	23.0	23.5
Gross fixed investment	26.4	23.3	23.2
(In billions of CFA francs) ¹			
External sector			
Exports, f.o.b.	1,506.6	1,567.3	1,475.6
Imports, f.o.b.	499.5	492.2	471.8
Current account balance (including public transfers)	-64.7	-6.9	6.0
External public debt service before debt relief (in percent of exports of goods and services)	23.2	22.9	16.8
External public debt (in percent of GDP)	196.3	179.1	184.7
Nominal effective exchange rate	1.0	2.1	4.3
Real effective exchange rate	-0.4	3.5	6.1
(In percent of GDP) ¹			
Financial variables			
Central government revenue	30.9	27.4	30.1
Total expenditure	31.6	35.4	29.7
Overall balance (deficit -, commitment)	-0.7	-8.1	0.4
Primary balance (deficit -)	6.8	1.2	6.8
Change in broad money (in percent)	-22.8	13.1	-2.4

¹ Unless otherwise noted.

Statement by Damian Ondo Mañe, Executive Director for the Republic of Congo
June 10, 2004

I would like to express my appreciation to Fund management and staff for the support and valuable advice provided to my Congolese authorities in the design and implementation of their economic adjustment programs. The comprehensive staff report and the selected issues paper offer a useful guidance to my authorities for advancing economic adjustment and structural reforms.

The Republic of Congo, a post-conflict country, is emerging from a decade-long political instability, characterized by three successive civil conflicts in the 1990s. These episodes of political turmoil have entailed considerable costs to the country. They have imposed tremendous suffering on the population, in terms of loss of life, exodus of a portion of the population, and destruction of entire villages, exacerbating poverty and weakening key social indicators. They have inflicted serious damages to the economy and the basic infrastructure, and have led to a weakening of key institutions. Moreover, sanitary and health conditions have deteriorated and the country's external debt burden is heavy. Poor economic conditions have led to a significant impoverishment of the population, and the spread of the HIV/AIDS endemics and other diseases. In evaluating the Congo's economic performance, it is important to bear in mind these daunting constraints and adverse conditions.

Following the completion of a four-year transition period by end-August 2002, including the installation of democratic institutions, the signing of the peace agreements with rebel groups in 1999 and 2003, political stability and security have improved, contributing to the pick up of economic activity in the non-oil sector and to the deceleration of inflation. With the completion of the democratization process and peace in 2002, a new government began to implement a policy agenda known as New Hope (*Nouvelle Espérance*). In that context, the authorities adopted and implemented a staff-monitored program (SMP) in 2003, initially covering the first half of 2003 and then extended to September of the same year. Despite difficulties, the implementation of this program helped the authorities to make progress in improving transparency and governance in the oil sector. Important achievements include the completion of the audit of national oil company, SNPC, for 1999-2001, centralization of government revenue, non-contraction of new oil-collateralized debt, and the publication of oil sector data on an internet site (www.congo-site.cg). Also encouraging were the observance in the last quarter of 2003 of the basic primary budget balance objective and certification of government oil revenue by an external auditor.

In order to consolidate the positive results achieved in late 2003 and stabilize the macroeconomic environment, the authorities adopted and are implementing a new SMP, covering the period of January-June 2004. Up to April 2004, the implementation of quantitative and structural indicators is broadly satisfactory. The authorities are determined to place poverty reduction at the center of their medium-term strategy. In this regard, an interim poverty reduction strategy paper is at an advanced stage of preparation, and is being conducted through a participatory process.

With the return of more stable conditions, my authorities are determined to strengthen the adjustment process and establish a strong track record under the 2004 SMP. Their aim is also to enable the Republic of Congo to receive Fund support under the Poverty Reduction and Growth Facility (PRGF), and to qualify for assistance under the Heavily Indebted Poor Countries (HIPC) Initiative, so as to bring the country's heavy debt burden to sustainable levels, and increase pro-poor outlays. To help them achieve their objectives, both technical and financial assistance from the international community will be of critical importance.

I. Recent developments and performance under the 2003 SMP

Developments on the political and security front are encouraging. The political transition period, which started at the end of the war in 1997, was completed in August 2002, after the presidential, legislative and communal elections. A peace agreement was signed between the government and the remainder of the rebel groups in March 2003, pursuant to which demilitarization, demobilization, and reintegration operations of former combatants started. With the improvement in security, displaced persons have returned to their villages, and all sites for internally displaced people were closed in May 2004. My authorities are appreciative of the support received from multilateral, bilateral and non-governmental organizations for care and resettlement of these persons. Moreover, the railway service between Pointe-Noire, the main sea port and Brazzaville has resumed its normal activity. To consolidate the gains being made and ensure lasting political stability, the authorities are strengthening the institutional framework, through the establishment of the Audit Office, the Economic and Social Council, and the Constitutional Court.

Economic activity in the non-oil sector continued to be strong in 2003, driven by favorable developments in agriculture, forestry, trade and transportation. Non-oil real GDP increased by about 5.3 percent in 2003. With regard to the oil sector, high world prices have compensated for the decline in production, leading to an increase in the government oil revenue. These additional resources were used to finance urgent reconstruction needs. Inflation decelerated to 1.2 percent from 3.1 percent in 2002, reflecting the recovery of food production; the regular supply of consumer goods, attributable to the resumption of rail traffic between Pointe-Noire and Brazzaville; and the strengthening of the euro. Moreover, for the first time in three years, credit to the private sector increased faster than non-oil GDP, reflecting a catch-up to a more reliable economic activity.

Fiscal performance improved in 2003, although it remained below the objective of the approved budget. The basic primary surplus increased from 1.2 of GDP in 2002 to 6.8 percent in 2003. This encouraging upturn was due to lower-than-expected expenditures and higher-than-expected oil revenue, leading to a significant improvement in the overall fiscal balance in 2003. Moreover, the authorities have taken corrective measures to address difficulties encountered in the collection of non-oil revenue and the management of treasury resources.

The **monetary policy** implemented by the regional central bank, BEAC, has served the country well. Reflecting a pickup in non-oil sector activity, credit to the economy increased at a faster rate than non-oil GDP growth for the first time in three years. The recent

privatization of the remaining state-owned bank, Crédit pour l'Agriculture, l'Industrie et le Commerce (CAIC), together with the expectations that activity in the non-oil sector will continue to improve, augurs well for ensuring a healthy banking system in the Congo.

Regarding the **external sector**, the Congo's external debt, currently estimated at 185 percent of the GDP, remains a heavy burden on the country's limited finances. Moreover, two-thirds of the external stock of debt represents arrears. Despite their limited resources, the authorities have started to normalize relations with external creditors, notably by remaining current on debt-service payments to multilateral institutions and Paris Club creditors on post-cutoff-date debt, and by clearing arrears to a few multilateral creditors.

Although **performance in 2003 as a whole** under the SMP turned out to be less favorable than projected, the authorities took steps during the last quarter of 2003 to stabilize the fiscal position and made progress in implementing structural measures. On the fiscal front, the objective set for the basic budget balance, which was revised downward, was attained. In order to ensure the payments of pension arrears and to cover the costs of structural reforms, the authorities were induced to carry out some additional spending. On the structural front, the authorities completed the certification, by an external auditor, of government oil revenue for the period January-September 2003. Other actions taken included the appointment of new directors in the General Directorates of Budget, Customs, and Taxes, as well as at the General Inspectorate of Finance; the signing of agreement among the government, SNPC, and CORAF, to have the latter pay for its purchase of government crude oil; and the production of the 2000 budget review law. All these actions go in the direction of improving the tracking of government revenues and enhancing governance.

II. Economic program for 2004

For 2004, the focus of the authorities is on putting the economy on a sustainable path of growth and poverty reduction in the context of an arrangement under the PRGF. In this connection, the authorities are implementing a new SMP covering the period January-June 2004. The main objectives of this SMP are to strengthen fiscal discipline and transparency in fiscal management, particularly in the oil sector. In the area of public finance, the key objectives are to ensure full revenue centralization and enhance expenditure control. The authorities are determined to improve the health of public finance, so as to create appropriate conditions for more effective fiscal management over the medium term. In the context of the SMP, efforts will be intensified to complete the restructuring of the banking sector.

The 2004 macroeconomic objectives are as follows: real economic growth of 3.6 percent, a rate of inflation of 2 percent, a basic primary fiscal surplus of 5.8 percent of GDP. The current account is expected to remain roughly balanced.

Fiscal policy

For 2004, fiscal policy aims at fostering discipline in public finance management. On the revenue side, the authorities are committed to ensuring that all revenue payable to the state is immediately transferred to the treasury. In this regard, they have continued the

certification of oil revenue by an independent auditor. Measures are also being taken to achieve a sustained increase in non-oil revenue. The implementation of a customs warehouse control program has begun. The authorities are also taking the necessary steps to develop a better identification and monitoring of large taxpayers, and modernization of management of customs and tax administrations.

On the expenditure side, the authorities are taking steps to ensure strict adherence to budgetary procedures. In this regard, efforts are ongoing to strengthen control over outlays, while ensuring that poverty reduction expenditure is protected. However, total traditional transfers are expected to record an important increase relative to 2003, due to the establishment of new institutions in support of democratization, including the Audit Office, the High Court of Justice, the national Commission on Human Rights and the Economic and Social Council.

To improve the social environment for productive activity, the authorities signed with labor unions a “social truce”, which will allow a gradual payment of wage and retirement pension arrears to begin in 2004. Moreover, the Treasury is being strengthened with expertise provided by the French Cooperation on public accounting. The authorities will gradually introduce a functional classification system for expenditure that will permit the allocation of a greater portion of public spending for poverty reduction programs. For the future, they will avoid procyclical fiscal expenditures related to oil revenue. In this connection, starting in 2005, the authorities will adopt a fiscal rule under which oil revenue will be projected on the basis of a conservative projection of oil prices.

Monetary and financial issues

Monetary policy will remain consistent with the objectives of preserving the exchange rate arrangement under the currency union and maintaining adequate level of reserves, while containing inflation. The expansion of credit to the economy is projected to meet the increasing needs of the private sector.

With regard to financial sector, besides the recent privatization of the CAIC, a reform of the insurance sector is also envisaged, with technical assistance from the World Bank. The role of the microfinance institutions in the expansion of the private sector will be enhanced. The authorities have launched a series of seminars to assist this sector in complying with the new regional regulations.

External debt

Based on a preliminary analysis, the Congo's debt burden, at 185 percent of GDP, even after application of full traditional Naples terms rescheduling, will remain unsustainable. While my authorities are committed to a prudent debt management policy, they will be unable to service their external debt's obligations fully. My Congolese authorities are hopeful that they could benefit shortly from the HIPC Initiative. In the meantime, they are making every effort to remain current on their nonreschedulable debt

obligations and, to the extent allowed by higher-than-projected oil prices, to make payments to reduce the large stock of outstanding arrears.

Implementation of the SMP during the first quarter of 2004

The implementation of the SMP through end April 2004 remains broadly satisfactory, both in terms of quantitative and structural indicators. Noteworthy are the fact that the primary fiscal balance was met by a comfortable margin, due to higher-than-projected non-oil revenue and enhanced expenditure control, and that no new arrears were accumulated. On the structural front, the authorities have made progress in publishing information, on the internet, of full report on oil revenue reconciliation for the first half of 2003, the SNPC action plan, and summary of the report on the 1999-2001 audit of the SNPC. They continue to take additional steps to strengthen transparency, and enhance policy credibility. My authorities remain committed to ensuring a good implementation of all measures envisaged under the SMP.

III. Governance issues

The authorities have taken important steps to strengthen transparency since 2003. In this context, it is important to note that the authorities carried out a corruption survey, commissioned a study on the issue and organized a seminar with the participation of officials, experts and representatives from civil society and the international donor community. Based on the views expressed at the seminar, the authorities are in the process of establishing a National Anti-Corruption and Anti-Fraud Commission. Under the chairmanship of the President of the Republic, this commission would monitor the implementation of anticorruption policies; centralize all information necessary, in order to assist government agencies or enterprises in tackling corruption.

IV. Poverty alleviation and medium term strategy

A poverty reduction strategy is under preparation and is at an advanced stage, and should become an integral part of the authorities' medium-term economic strategy. The main objectives of this strategy will be to stimulate a sustained growth and to promote development centered on the poor. It is the authorities' intention to promote growth that will generate employment and resources that will benefit a large portion of the population. Moreover, my authorities are also committed to promoting the development of private sector activity, mostly in the non-oil sector.

Constraints to economic development are related to high dependence on oil, weak infrastructure, heavy public debt burden, high cost of public utilities, and low degree of financial depth. The legacy of central planning and the associated anti-business bias have also been a cause of severe constraint. Moreover, the civil wars of the 1990s, which affected the economy, weakened the institutions and undermined the rule of law. The authorities have begun to address these problems and important progress has been made. These constraints have also been a source of program failure in the past, but all these are in the process of being changed, with the economy moving gradually but steadily towards a market economy. The

authorities have learnt lessons from these past experiences and are determined to take necessary steps to create conditions for broad-based economic growth and poverty alleviation.

V. Regional integration

Being a member of the CEMAC, Congo has met two convergence criteria, namely the basic balance-GDP ratio and inflation rate. However, it has missed the remaining two criteria related to public debt-GDP ratio and net change in arrears in government arrears-GDP ratio. On the integration of product markets, key actions undertaken were the promulgation of the CEMAC's investment charter and the issuance of two implementing regulations. The National Law on Investment is expected to be revised, in compliance with the CEMAC charter, by the end of this year. Congo remains in compliance with the implementation of the regional customs code. The authorities have also established the national financial intelligence unit that is in charge of coordinating regional efforts to combat money laundering and the financing of terrorism.

VI. Conclusion

My Congolese authorities have made significant efforts to emerge from a post-conflict situation. Remarkable achievements towards peace and political stability have been made. My Congolese authorities are committed to continuing to work closely with their partners to help them achieve the goals of sustained growth and poverty alleviation. The results achieved up to now under the 2004 SMP are encouraging and reflect the authorities' firm determination to restore fiscal discipline. However, strong support from the international community remains critical for the consolidation of the progress achieved. In this context, they hope that their efforts will be well recognized and will help to pave the way for Fund support under the PRGF, which will be the basis for the creation of a solid foundation for economic development and poverty reduction.